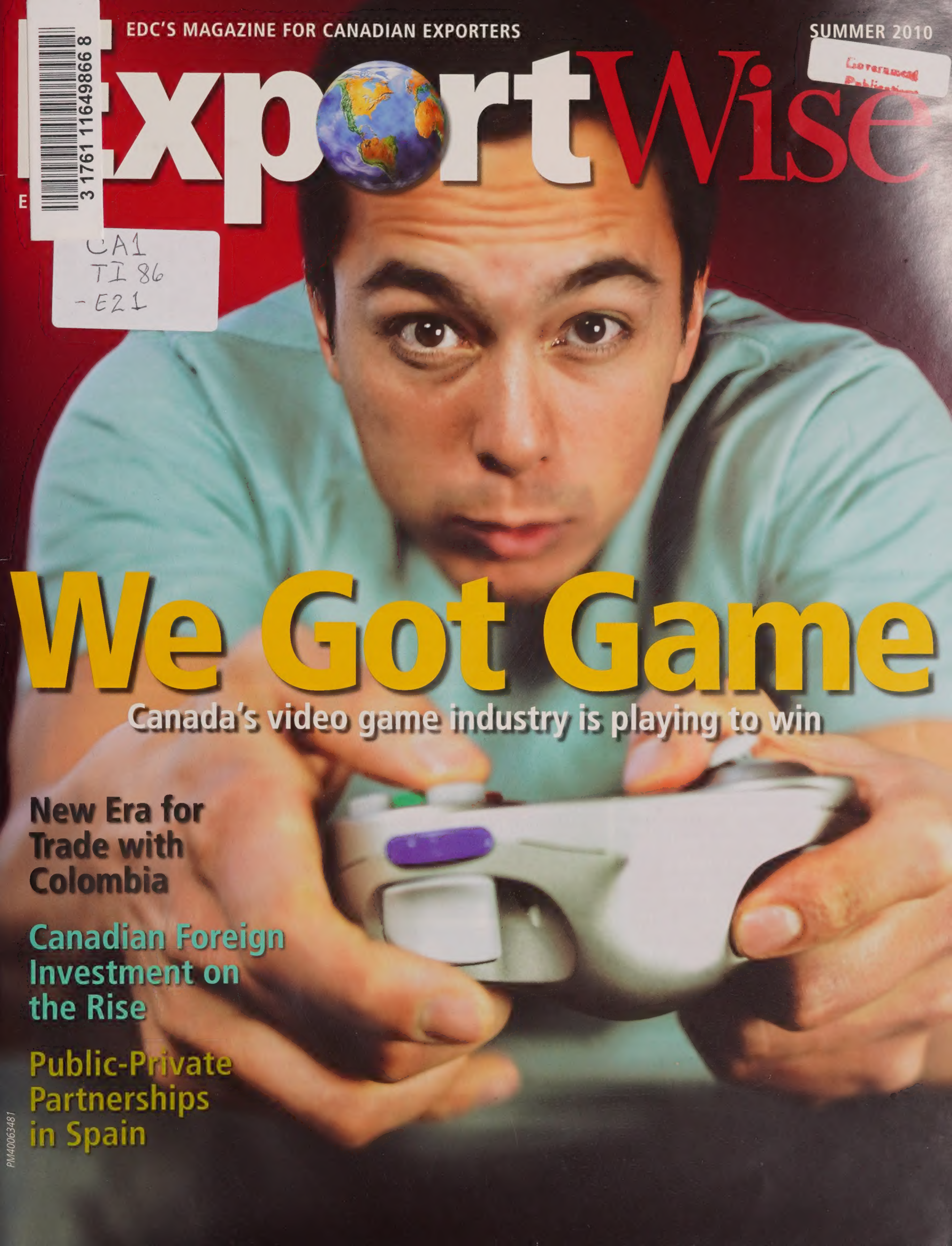
EDC'S MAGAZINE FOR CANADIAN EXPORTERS

SUMMER 2010

ExportWise



We Got Game

Canada's video game industry is playing to win

New Era for Trade with Colombia

Canadian Foreign Investment on the Rise

Public-Private Partnerships in Spain

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Eric Siegel President & CEO

Canadian Industry Gets Creative

When most people think of Canadian industry, they think of Canada's corporate heavyweights in the resources, engineering and aerospace sectors. So you may be surprised to learn that the vast majority of EDC's customers – 83 per cent in 2009 – are small and medium-sized businesses. Their stories may not always make headlines, but their creativity and innovation are at the root of Canada's prosperity.

Canada's rich resources are in great demand worldwide. EDC works closely with Canada's exporters in traditional industries: oil and gas, mining and forestry. Last year, EDC supported almost $40 billion in business in these sectors – almost half of our total business.

But while these industries are the mainstay of our economy, it's important to recognize that Canada's economy is becoming more diverse and innovative, and EDC is supporting that transition.

In this issue of *ExportWise*, you'll read about some of the companies that are keeping Canada at the cutting edge – companies like London, Ontario-based video game developer Digital Extremes, which partners with global leaders like Electronic Arts, Sony and Microsoft. Canada has a wealth of expertise in communications technologies and new media, from household names like Research in Motion to smaller companies like Commport Communications International, which is cornering a niche market for fuel management systems.

Even within traditional resource-based industries, it's no longer simply the export of raw materials that is guiding Canada's future; it's the expertise we've gained in developing those resources. Take, for example, St. John's Pan Maritime Energy Services, which is taking its project management and engineering services in the oil and gas industry to the Middle East. Or Red Deer's Canalta Controls, which is manufacturing industrial control and measurement equipment for oil and gas companies from Venezuela to Indonesia.

And EDC is doing its part to ensure we have a diverse range of products and services to support these innovative Canadian companies as they look for opportunities abroad. While credit insurance is still the biggest part of our business, we're working hard to get to know all of our customers' needs and introduce them to the full range of EDC risk and financial management tools that can help them grow.

It's important to recognize that Canada's economy is becoming more diverse and innovative, and EDC is supporting that transition.

We're also making sure our customers know about our network of international representatives and partners, and the opportunities we are developing in emerging markets. We're helping companies to move beyond exports, supporting more Canadian Direct Investment Abroad (CDIA), which helps companies to become part of global supply chains and benefit from the strong growth in these markets.

We're also continuing to grow our equity investment program, through which EDC invests in a variety of professionally managed funds that provide venture capital. Our equity investments are focused on funds that support exporters of next generation technologies, as well as those that target connections that can help Canadian companies find opportunities in emerging markets.

EDC's equity investments reached a total of $700 million in 2009, up from $224 million in 2008. Given the constrained credit market that businesses have faced in the past year or two, this program is playing a particularly important role in helping small and mid-sized companies access the private equity and venture capital they need.

For example, in 2009 EDC announced a $75-million investment in the Tandem Expansion Fund I, which will focus on growth capital for high-potential Canadian technology companies. Most recently, we announced an investment of up to USD 20 million in the Africa Telecommunications, Media and Technology Fund, which will help encourage Canadian supply to the burgeoning communication technology sector on the African continent.

Thousands of innovative small and medium-sized Canadian companies are developing superb products and services and taking them to world markets. EDC recognizes that creative, entrepreneurial Canadian companies are the driving force behind Canada's competitiveness, productivity and living standards, and we're working hard to help them succeed as the next generation of Canadian world-leading corporations. ■

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Summer 2010

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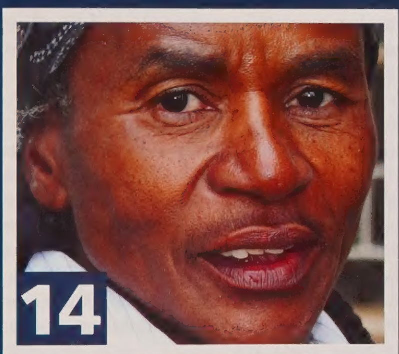
COVER STORY › Canada built a $1.7 billion video game development industry with global markets



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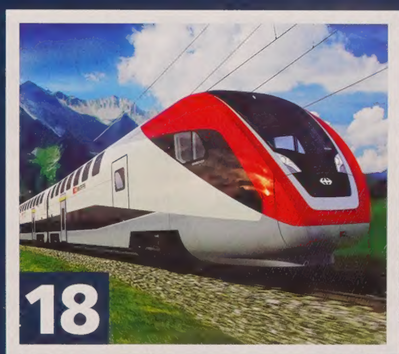

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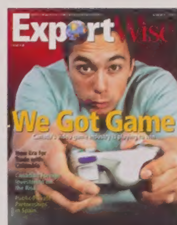

This is the second in a series of articles examining public-private partnerships (PPPs) and how they function abroad. In this instalment, we'll look at Spain's PPP model and the opportunities for Canadian companies in the Spanish and EU markets.

A Better Way to Build

Understanding Public-Private

Part 2: Spain

BY DENNIS AND SANDI JONES

Since Spain joined the EU in 1986, its national and local governments have worked hard to improve the country's productivity, foster its economic growth and improve the quality of life for its citizens. Much of this effort has been devoted to rebuilding the nation's infrastructure – and often creating new infrastructure as well – to strengthen the foundations of its economy.

The scale of the Spanish PPP market is huge, with more than €240 billion worth of projects planned or in development between 2005 and 2020. About a third of the country's highways now operate under PPP arrangements, and the use of PPP has expanded into other infrastructure sectors including railways, ports, airports and hospitals. Many of these projects have been undertaken by the central government, but the country's regional and municipal governments have accounted for a large number of them as well.

Many of these projects, and the opportunities associated with them, are the outcome of Spain's Strategic Plan for Infrastructure and Transportation (PEIT). This program, which was launched in 2005, commits very large sums to new and improved highways, railways, airports, ports and other infrastructure.

"PEIT forecasts a total investment of €241.4 billion over 15 years," says Jorge Del Solar, a project director for Acciona, a century-old Spanish company that is now a major force in the global infrastructure, energy and water sectors. "Within that investment is a €17 billion infrastructure spending plan that was announced early in 2010 and will continue into 2011. This latest spending will support PPP contracts for construction work on highways, on high-speed rail and rail cargo projects, and on social infrastructure such as hospitals and schools."

In the larger perspective, this two-year program is intended to help the Spanish construction sector weather the current financial crisis by attracting private investment, and to allow the government to maintain its public works tendering even as it cuts its infrastructure spending.[1]

Spain's evolving PPPs

The structuring of Spanish PPPs has evolved along with the laws affecting them. Until recently, the most common structure was the concessional model, in which the private entity (the concessionaire) builds, finances and operates the facility for the public partner, and is paid via the operating proceeds. However, some kinds of projects – healthcare facilities, schools, prisons and government office buildings, for example – do not fit very well with the concessional approach.

[1] According to a May 2010 statement by the Minister of Public Works, however, Spain's current austerity program will cause the government to miss at least some of its current PEIT targets.

What are PPPs?

In general, PPPs – or P3s, as they are called in Canada – are long-term contracts in which the public sector procures the design, construction, operation and/or maintenance of an asset from a consortium of private firms, with the acquisition being privately financed over the economic life of the asset. These assets are almost always large infrastructure facilities such as roads, bridges, railways, hospitals and schools. Typical PPP contracts run for 20 to 30 years, but can be even longer for some types of projects.

The practical details of each country's PPP approach – such as financial structuring, risk allocation or ownership of the asset – can vary according to local preferences and needs, but all are based on the general model described above.

Villafranca Motorway in Aragón, Spain – Concession for the design, construction, financing and operations of a shadow toll motorway.

In an attempt to rectify this, the Public Sector Contracts Law of 2007 extensively revised the structure and content of Spanish public procurement regulations and established a new form of contract specifically for PPPs. This development will make it easier to apply PPP approaches to a broader range of projects.

Before a project can be undertaken as a PPP, however, the public partner – which may be a state, regional or municipal government – must show that its complexity justifies the PPP approach, that the public partner lacks the technical and financial resources to carry out the project on its own, and that a PPP will provide better value for money than a conventional contract. Somewhat curiously, given its long history with PPPs, the Spanish government has not established a dedicated PPP unit that can support open competitions for complex PPP projects at the various levels of government. In contrast, all the other EU members have such units, and Canada has both the federal-level PPP Canada and several provincial PPP entities.

EDC has been involved with PPPs since 1997, and has worked with the various kinds of PPP models used in the Western and Eastern Europe, the U.S., the Middle East, Latin America and the Caribbean. EDC has acted as Mandated Lead Arranger and Co-Arranger on a series of projects including, for example, PPP projects that outsourced various Ministry of Defense training programs in the U.K.

EDC has been involved with PPPs since 1997, and has worked with the various kinds of PPP models used around the world.

Practical structuring

At the practical level, most Spanish PPPs are structured in one of two ways:

- In the first approach, the public and private partners either create a joint entity to carry out the project, or the private partner assumes a stake in a pre-existing public project.
- In the second approach, no joint entity is created. Instead, the public and private partners cooperate on a purely contractual basis. This contractual model usually takes one of two forms:
  - The private partner secures a concessional contract to build and operate a facility for the public partner, and the concessionaire deals directly with the facility's end users. One example of such a facility would be a toll highway.
  - The private partner contracts to build and manage a facility for the public partner, but the public partner delivers the required service. The private partner has no direct link to the end users. A hospital would be such a facility.

Financing Spanish PPPs

Another practical outcome of the 2007 law is that it encourages the use of service *output* specifications – such as providing health services for a community of 50,000 – when developing the requirements of a PPP. This is a departure from traditional Spanish practice, in which the public partner issues the technical *input* specifications for a PPP project, such as the specific materials and equipment to be used in building the facility. The service output approach is preferred in both Canada and Great Britain, where governments decide what services they will provide for the public, but leave the private partners to determine how best to deliver them. As Spain moves closer to the latter model, it is likely that PPPs will increasingly substitute the service output specification for the technical input specification.

"In recent years," says Del Solar, "private financing has made up 20 to 30 per cent of equity, depending on the kind of project and the level of risk assumed by the private partner. The debt term does not usually exceed 25 years, and there can be some different financing tranches depending on capital grants and other factors."

Under a Spanish concession contract, a public work must be financed by the concessionaire, who bears any financial risk involved. Private financing is also the usual source of money for PPP projects that involve the participation of publicly owned companies. Under special conditions, though, public

Photo: Courtesy of Acciona

Navarra, Spain – Concession for the design, construction, financing and exploitation of the infrastructure for the irrigable area of the Navarra Channel.

financing such as subsidies or loans may also be used for PPP projects, especially when they are related to social and public needs.

Unfortunately, the EU's embroilment in the global financial crisis has made it more difficult and expensive to obtain private long-term financing for Spanish PPP projects. As a result, the volume of PPP spending in the country has dropped substantially as sponsors and bankers have lost their inclination to take risks. The most recent PPP toll highway structuring was 60 per cent debt to 40 per cent equity, with a tenor of 7.75 years, which is not an ideal arrangement for this kind of project.

None of this is to say that funding has dried up, however. The €17-billion infrastructure spending plan mentioned earlier, for example, is obtaining 20 per cent of its financing from private sources.

Risk and ownership

On the risk side, EU membership requires that a country's debt not exceed 60 per cent of GDP, a principle that limits the ability of an EU country to borrow money. The Spanish government, for instance, cannot borrow the cash to build a highway or hospital if the loan would push the country's total debt over that limit.[2]

Such projects can be feasible, however, if they are carried out as PPPs. This is because the assets linked to a PPP are not used in calculating public debt, provided that the private sector

[2] In June 2010, however, EU authorities agreed to use debt *trends* to control public debt, rather than the rigid 60 per cent ceiling. A country with a debt above the ceiling would not be penalized as long as its total debt was trending downward.

PPP COMPARISONS

	CANADA	UNITED KINGDOM
Major opportunity sectors	Roads, bridges, hospitals, community facilities	Roads, bridges, hospitals, schools, prisons, railways, airports, ports, urban transit, government and community facilities
Dedicated PPP entities	There is a federal Crown corporation (PPP Canada) and several provincial entities	Partnerships UK operates at arm's length from HM Treasury to support the use of PPPs in the U.K.
Strategic approach	Uses service output specifications	Uses service output specifications
Structuring	Primarily the design-build-finance-manage model, or the design-build-finance-operate model	Primarily the design-build-finance-manage model, or the design-build-finance-operate model
Financing	A substantial share of a Canadian PPP is privately financed through project-specific equity and debt. Third-party debt, bank loans and contributions from governments provide the balance.	Typically uses private financing, but there can be a mix of government money, private debt, equity investments, bank loans and sovereign wealth funds
Bonding	Surety bonding or a combination of surety bonding and standby letters of guarantee	Standby letters of guarantee; surety bonding is not used
Recent financing measures	The federal government launched "P3 Canada Fund" in 2009 to invest in PPPs	As of late 2009, HM Treasury can provide up to 100% of debt, on advice and input from Infrastructure UK
Risk allocation	Depends on project	Depends on project
Ownership	Reverts to public sector on contract completion	Reverts to public sector on contract completion
Bidding process	Multi-stage	Multi-stage
Entry strategy	Partner with or establish local consortia	Partner with local consortia

assumes an adequate amount of the overall project risk. Since PPPs are inherently designed for such risk transfers, especially if they are concessional, using them can allow the public entity to avoid the EU constraints on the level of public debt.

In Spain, as in the rest of the EU, there are three major types of risk applicable to PPPs:

- construction risk, such as delivery delays, failure to fulfill contract criteria and technical defects;
- demand risk, such as falling levels of demand because of market or other economic conditions; and
- availability risk, such as a failure to deliver the contractually agreed level of service, or a failure to meet quality standards.

These risk categories are used when calculating whether the debt incurred by a project would increase the overall public debt above EU limits. If the construction risk is transferred to the private partner, and *either* the demand risk *or* the availability risk is also transferred to the private partner, the PPP's assets are not included in the calculation and the public debt does not increase.

"The details of the actual risk sharing depend on the contract," adds Del Solar, "but the current tendency in Spain is to assign the availability risk to the private partner, with high penalties if the required quality of service is not delivered. The construction risk is always assigned to the private partner."

As for the ownership of a Spanish PPP project, where does that lie both during and after the term of the contract? "The final owner of the asset, and the one with the ultimate responsibility for it, is the state, regional or municipal administration," says Professor Antonio López Corral, a specialist in PPP studies at the Polytechnic Institute of Madrid. "During the concessional period, however, the private partner is the economic owner."

SPAIN
Roads, bridges, hospitals, community facilities
No central PPP unit has been set up to provide support for negotiating complex PPP projects
Traditionally has used technical input specifications, now moving toward service output specifications
Primarily the concessional approach, where the concessionaire builds, finances and operates the facility, and is paid via the operational proceeds
Concessionaires are fully responsible for obtaining financing and assuming the risks thereof. Primary source of financing is usually bank debt, mainly as project finance.
Standby letters of guarantee; surety bonding is not used
Various public-sector financial stimuli have been put in place by central government to sustain the infrastructure sector
In concessions, the private partner must assume all construction risk plus either availability risk or demand risk; expropriation risk is a major issue
Reverts to public sector on contract completion
Open competition, single-stage
Partner with local consortia

Spanish strengths

The long cooperation of Spain's private and public sectors in scores of PPP projects means that its companies have developed a great deal of expertise in the construction, renewal, maintenance and operation of public infrastructure across many sectors, especially in the area of transportation. The contractual and bidding processes for new PPPs are also highly streamlined, partly because public procurement in Spain is closely regulated. Most elements of a procurement contract are legislated by the state, which means that there is little need or opportunity for lengthy, clause-by-clause negotiation.

The second streamlining factor is that the Spanish bidding process consists of a single stage, with no short-listing or pre-qualification – multiple bidders submit binding bids and the government selects a winner, mainly on price. This is distinctly different from the Canadian and British multi-stage approach, which requires an expression of interest, a request for proposal, the selection of the preferred bidder and the final, pre-award contract negotiations. As a result, a Spanish bid submission takes three to four months, about half of what is needed in Canada.

It is worth noting that some of the current decline in Spanish PPP activity has been caused not by the financial crunch, but by the fact that so much of the country's infrastructure has now been upgraded or replaced. Both factors are contributing to an increased Spanish interest in foreign PPP markets, which is why some Spanish consortia have begun to compete for Canadian projects.

Entering the Spanish PPP market

Participation in Spanish PPPs is not limited to Spanish or EU consortia – Canadian companies are welcome to become involved, assuming they have the qualifications to do so. It is an extremely competitive market with many local players, however, and internal rates of return (the annual effective compounded return rate) tend to be very low.

As for identifying opportunities, the *Official Journal of the European Union* lists all the major tenders on offer in the EU, including PPPs. These listings provide instructions and information about tendering, bid specifications, prequalification, eligibility and other essentials. Other online journals, such as *Project Finance Magazine* and *PPP Journal*, are useful sources as well. The official journals of the Spanish regions, municipalities and the central government also publish PPP tendering requests, and there are various organizations, such as the International Project Finance Association, that offer specialized information on a subscription basis.

"To participate in the bidding process," says Professor Corral, "a Canadian company will need to become part of a consortium. That is the major challenge; the competition here in Spain is very strong and there may be as many as 10 different consortia bidding on a project, but at the same time, the market is very open. The best way to enter it is to form an alliance with a local company that knows how the Spanish PPP market works. Your partner can then evaluate your qualifications for the project, represent your firm to the consortium's existing partners, and help you make your case for inclusion." ■

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Canadian Foreign Investment on the Rise

Graphic: ©iStockphoto/Vlad Konstantinov

BY ERIC BEAUCHESNE

Canadian exporters are increasingly, and successfully, setting up shop abroad to boost sales, tap into global supply chains, cut costs and become more productive and competitive, new research by Export Development Canada reveals.

"Canadian companies are working hard to adapt to a more integrated world economy and a more aggressive business environment," concludes an analysis of an EDC survey of exporters' views towards and experiences with Canadian direct investment abroad (CDIA). "Investing outside Canada is one strategy that companies of all sizes are using to respond to these challenges."

About one-quarter of the 274 small, medium and large firms surveyed engaged in CDIA, while another 25 per cent were seriously considering such an investment within 18 months, the survey found. The March survey is part of a broader EDC effort to encourage CDIA by gaining a better understanding of why exporters make – or don't make – such investments, and helping firms overcome challenges they may face in doing so.

Why Canadian companies invest abroad

Increasing their sales, cited by two-thirds of those exporters with existing CDIA experience, is the most important reason for establishing a foreign affiliate or entering into a joint venture with a foreign firm, both of which are forms of direct investment.

"There are also the benefits that come from the earnings that are repatriated by Canadian firms, including the increased research and development, higher value-added employment, and the generation of tax revenues," says Stuart Bergman, director of Economic Analysis & Forecasting at EDC. "CDIA is also a way to develop new export markets, by gaining a foothold and introducing Canadian products into those markets."

Other motives are to better service existing customers, enhance competitiveness in a foreign market or global supply chain, enter a new market, gain cheaper access to resources or labour, reduce transportation costs, be part of a new regional or global supply chain, mitigate the impact of the strong Canadian dollar, secure a supply of resources, gain access to new technology, and follow buyers who have invested abroad.

12 reasons companies invest abroad

To increase sales	66%
To increase market share in an existing foreign market	58%
To better service existing foreign buyers	46%
To enhance our competitiveness within an existing regional or global supply chain	40%
To enter a new foreign market more effectively than through exporting	35%
To gain access to resources (physical, human, etc.) at a lower cost than in Canada	27%
To reduce other costs (transportation, customs, duties, etc.)	27%
To be part of a new regional or global suppply chain	19%
To mitigate the impact of a strong Canadian dollar on our company's competitiveness	16%
To secure sources supply (e.g. raw materials)	14%
To gain access to new technology	8%
To follow buyers that have decided to invest abroad	6%
Other	4%

Canadian foreign investment is growing

While 16 per cent of exporters who engage in CDIA, and fully one-third of those seriously considering it, see it as a way of cushioning themselves against the impact of the strong Canadian dollar, the strength of the currency has also made foreign investments cheaper.

Meanwhile, the stock of CDIA has increased 65 per cent over the past decade to $593 billion in 2009 from

$360 billion in 2000. Since the Canadian dollar was stronger in 2009 than in 2000, the rise was actually more pronounced than what the data shows.

The increase in CDIA is part of an even greater surge in global foreign direct investment flows to an annual level of US$1,700 billion in 2008 from US$200 billion in 1990, notes Jean-François Lamoureux of EDC's Corporate Research department.

"Worldwide we are seeing investment increasing," he says.

The growth of such investment globally is expected to continue, despite some short-term deceleration resulting from "hiccups" in the world economic recovery and global credit markets, adds Bergman.

Much of that growth will be fuelled by the development of an increasingly captive middle class in the emerging markets. Non-traditional markets themselves have become much more attractive places to invest, as globalization brings about improvements in communications and transportation infrastructure, he explains.

However, the EDC analysis says it is "somewhat disappointing" that just two sectors – energy and financial services – have accounted for 90 per cent of the growth this past decade, and that the share of CDIA in the rapidly expanding emerging market giants, the so-called BRIC countries of Brazil, Russia, India and China, has remained flat over the past two decades at just two per cent. The bulk of CDIA still goes to the U.S. – 44 per cent in 2009, though that is down from 50 per cent in 2000 and 61 per cent in 1990.

Investment in emerging markets allows Canadian firms to tap into that spectacular growth and also cushions them against the slower growth and recent weakness in their traditional market, the U.S.

"As we emerge from this downturn... the real winners are those that learn to sell their goods and services to the new drivers of the global economy," Bergman says, adding that direct investment in emerging markets establishes a platform from which firms can tap into those markets.

"The individual firm does, and will absolutely benefit going forward, from being able to plug itself into the new drivers of the global economy, not solely being focused on their traditional market, the U.S.," he says.

Why some companies aren't investing abroad

But just as there are numerous reasons for launching foreign direct investments, there are also reasons why nearly one-half of the exporters surveyed have not and do not plan such a venture, the survey found.

"Their reasons for not investing abroad include the risk of foreign trade, satisfaction with current returns and the existence of profitable exporting opportunities," the analysis notes. "Other factors are a lack of financing and shortages of competencies, information, knowledge and time."

Those exporters, however, may want to reflect on the success of others – many of them small and medium-sized firms – that have made direct investments abroad. The survey found that most had achieved their objectives.

"For example, 68 per cent of companies that had invested abroad to increase sales felt that they had achieved their goals," the survey analysis notes. "A further 24 per cent said they had been at least somewhat successful in increasing sales, while only six per cent said they had failed to do so."

EDC can help

Nonetheless, there are challenges to establishing a presence abroad, and managing one once it is in place.

The major challenges companies face prior to making a foreign investment include lack of financing, problems with finding local business partners, and the difficulties of obtaining information about local business environments and the procedures for establishing companies within them, the analysis points out. Companies also encounter problems when trying to find domestic Canadian resources to help them set up their foreign investments and identify local suppliers, distributors and legal counsel.

After the foreign investment has been made, the main challenges lie in dealing with the local bureaucracy and the time commitment that the investment requires from the Canadian management side. Other problem areas are local workforce management, partner relationships and compliance with local laws and regulations.

Bergman points out that EDC has the expertise to help firms deal with the challenges of setting up and managing an investment abroad.

"We have people on the ground that can put businesses in touch with local agents and partners to help them navigate the bureaucracy and deal with the legal framework," says Bergman.

"We have in-house experts here to speak to the risks of those markets. We have an entire team devoted to political risk analysis and one devoted to economic risk analysis, not to mention teams that deal with the other operational risks that a Canadian investor may face. So we have the expertise to demystify these markets."

The survey of exporters was conducted using the EDC Online Research Panel which was launched in the spring of last year. It is an online community of almost 1,200 representatives of Canadian businesses involved in international trade who have volunteered to share their insight and experience with EDC.

"Through regular, short, online surveys, we seek to understand the challenges Canadian businesses face and, ultimately, serve our customers better as a trusted partner," says Alberto Vargas, Strategic Marketing Research Manager at EDC. ■

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Many Canadian companies have cited cultural hurdles and concerns about intellectual property rights infringement as obstacles to engaging in CDIA in Asia – especially in China. However, investors from other markets face the same challenges and it hasn't prevented them from investing heavily in Asia.

What do you think? Should these concerns be barriers to Canadian companies growing or maintaining our market share in Asia? What do you see as the key hurdle to investment in Asia?

Share your opinion at ExportWise.ca/CDIA

This Ain't Kid Stuff

Canada's Surprising Success in the Global Video Gaming Industry

BY DANNY KUCHARSKY

Photo: ©iStockphoto/Mike Sonnenberg

When video gamers face ominous virtual opponents they can zap them to kingdom come with one touch of a joystick. But for Canada's video game industry, which has produced many of the world's most successful games, it often takes much more than the press of a button to secure real-world financing when it's needed.

This, despite the fact that Canada's video game industry generated an estimated $1.7 billion in revenues in 2009 and employs about 14,000 people in 400 companies, primarily in Vancouver, Montreal and Toronto. The country is the world's third largest centre for video game development behind only the U.S. and Japan and is projected to grow 29 per cent annually over the next few years.

Twenty per cent of the top-selling games in North America were developed in Canada. Games such as Assassin's Creed, one of the most successful video games, are Canadian developments (in this case by Ubisoft in Montreal).

"If this was the film industry, we would have a big chunk of Hollywood in Canada," says Ian Kelso, president and CEO of the Ontario industry trade association, Interactive Ontario. "We have a lot of things going for us."

This includes generous tax credits and subsidies, first introduced in 1996 by Quebec with other provinces following suit, which have attracted some of the world's largest video game development studios.

But despite the success of the industry in Canada, one challenge remains: cash flow during the product development stage.

Global leader: Activision

"Jurisdictions like Quebec and Ontario have really been on the ball in terms of helping foster the industry," says Brian Ward, senior vice-president, worldwide studios at California-based Activision, the world's largest video game publisher by market value. For 2009, Activision's revenues were $4.3 billion, 52 per cent of which came from North American sales, while 42 per cent of sales came from Europe and 6 per cent from Asia Pacific.

Activision created the games Call of Duty and Modern Warfare 2, which generated an estimated $1.3 billion in worldwide sales. Besides operations in the U.S. and Canada, Activision has studios in the U.K., Ireland and China.

Thanks in part to Canada's tax credits, Activision operates video game development studios in Quebec City (Beenox) and Vancouver (Radical) that makes Monsters vs. Aliens, Bee Movie and Prototype games. The Quebec City studio has grown from 29 employees working on development when it was acquired by Activision in 2005, to 180 today. In addition, Activision created 350 quality assurance jobs in Quebec City, most of which were previously in California.

"For the size of the country, Canada has a very robust video game development community."
Brian Ward, Activison

"It is fantastic," says Ward of the quality of work produced in Canada. "For the size of the country, Canada has a very robust video game development community. Canadian developers grasp the business end of it as well as anyone else."

Aside from work produced by its own studios, Ward says Activision also has about 20 projects in development with independent studios around the world, including United Front Games, Next Level Games and Silicon Knights in Canada.

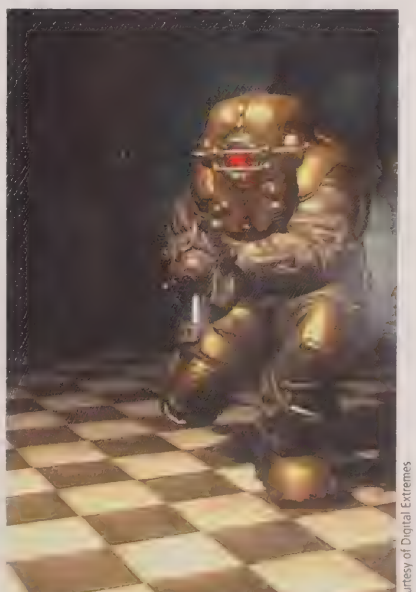
Ward says Vancouver is one of the few development centres in the world where there are still several top independent developers. He says this is a key advantage, because it allows publishers like Activision to work with new development talent. As well, several of the independents are owned or founded by entrepreneurs who, if they sell their firms, will create successful new companies.

However, despite generous tax credits, Canada's industry faces a number of financial gaps which EDC is now setting out to bridge. "The video game industry is probably the most identifiable and strongest cluster within new media, and really represents a growth industry for Canada," says Robert Caouette, Sector Advisor, Information and Communications Technology at EDC. "It is an export ind try by nature, and has a critical mass Canadian exporters, so it just made sen for us to look into it."

Cash-flow challenges

EDC found the biggest problem in the industry is liquidity, Caouette explains. The work-for-hire business model is prevalent in the industry. Publishers – all based outside Canada – fund game development and hire Canadian game developers to develop games. In return for funding game development and overseeing distribution and marketing of the final product, the publishers retain intellectual property (IP). The publishers also control the games' digital distribution through consoles like PlayStation, Xbox and Nintendo.

Still, the publishers provide critical assistance to the success of any title, Kelso notes. "They have a vested interest in it and they go out and market it like crazy. Sometimes the marketing budgets are as expensive as or more expensive than the production budgets." (New platforms such as iPhone and Google Android games are also exploding and


Courtesy of Digital Extremes

BioShock 2 from Digital Extremes is the latest installment in the franchise that has won more than 50 Game of the Year Awards.

Canada's gaming sector

$1.7 billion revenues in 2009

14,000 jobs

3rd largest in video game development

29% projected annual growth

20% top-selling games in North America

these self-distributed platforms have created a myriad of opportunities for content creation and distribution, Kelso says. With these platforms Apple and Google are not acting as publishers, but as distributors and do not provide financing.)

Contracts between publishers and video game developers are milestone-based, meaning that developers don't receive payments until project milestones are fulfilled. In between, "there may be a gap of a few days to weeks where the Canadian game developer is forced to fund ongoing development," Caouette says. Uneven cash flow limits the number of projects a developer can take on at any one time and can affect talent retention.

As well, "publishers can cancel the contracts at any time for basically any reason," Caouette says, leaving Canadian companies stuck paying their staff with no revenues coming in. "With an unforeseen contract cancellation, you likely don't have anything in the pipeline that you can just quickly have your staff work on."

Kelso notes that at the outset of any project, developers take substantial risks when they're developing their prototypes and have to sink a significant amount of money just to pitch to publishers.

In addition to contracts "that put all of the power in the hands of the publisher," Caouette says the biggest challenge is that banks are taking a cautious approach which has resulted in a gap in financial support to the gaming industry. Often, banks are not aware of EDC's involvement in the industry and, as a result, EDC is not approached by the banks to provide financial guarantees. "For exporters, right off the bat, the bank says, 'You're in an industry that we're not really comfortable with.'"

> **"For EDC it's an opportunity for getting into a niche that we've not necessarily supported in the past," says Robert Caouette, EDC**

Born to export – Digital Extremes

That's a situation that is familiar to Michael Schmalz, president of Digital Extremes, a 110-employee game developer in London, Ontario. The company got its start in the early 1990s with the shareware game Epic Pinball that became one of the most successful shareware games ever. Over the years, Digital Extremes has partnered with Electronic Arts (EA), Atari, D3, 2K, Microsoft and Sony and others. About 97 per cent of the company's market is outside Canada. Digital Extremes is now best known for its various Unreal and BioShock games that have sold about 18 million copies combined.

Aside from generating continual profits, Digital Extremes made Canada's Top 100 employers list last year and was named one of the *Financial Post's* Ten Best Companies to Work For. It is now licensing its Evolution Engine software to other developers. Evolution Engine automatically detects errors in code as they are being made, eliminating problems as the game is developed.

Schmalz says traditional lenders have difficulty understanding the risks and opportunities in funding a $15 or $20-million project – the typical cost for making a large video game project for the Xbox 360 or PlayStation 3 formats. (Even more expensive are the $30 to $40-million budgets for Triple A games, based on such variables as critical acclaim and sales.)

In a few cases, banks have been willing to lend Schmalz a few million dollars. But his response is that amount represents only a few months of payroll. "You're giving me a boat that's got a leak in it, that will get me half way across the river. I've got to get to the other side of the river. Ultimately, those deals go nowhere."

FACTS about Canada's video game industry

- Almost half (48 per cent) of Canadian households have at least one video game console, such as an Xbox 360, PlayStation or Wii.
- 90 to100 per cent of the revenues of the Canadian video game industry are generated through export sales, according to an April report by the Entertainment Software Association of Canada.
- Six of the top 10 Canadian game developers are foreign-owned: EA Canada (owned by U.S.-based EA), Ubisoft Montreal (Ubisoft), EA Black Box (EA), EA Bioware (EA), EA Montreal (EA) and Beenox (Activision).
- Global revenues in the game industry are expected to reach US $68.4 billion in 2012.
- Annual growth in the industry is predicted to be most apparent in the Asia Pacific (10 per cent) and Europe/Middle East/Africa regions (10.2 per cent), followed by Canada (9.4 per cent), Latin America (9.2 per cent) and the U.S. (6.7 per cent).

Caouette says a challenge for banks (as well as EDC) is that the main asset of companies in this industry is their intellectual property (IP). "IP is probably the biggest asset on the game developer's asset sheet."

Cash-flow solutions

The reticence of banks to provide much financing may be aided by EDC's Export Guarantee Program, Caouette says. The program provides additional cash flow for developers throughout the game development cycle to compensate for delays in milestone payments. It could also allow developers to fund additional projects.

A program that could ease the gaps between milestone payments is encouraging to Schmalz. "It's always about getting money at the right time."

Under the Export Guarantee Program, EDC works with the game developer's bank to guarantee lines of credit or facilities that are being put in place by the bank on behalf of the exporter. "It gives the bank more appetite and ability to support Canadian game developers," Caouette says.

He adds that EDC is working with traditional lenders in an attempt to create awareness of EDC's involvement and support for the gaming industry. "For EDC it's an opportunity for getting into a niche that we've not necessarily supported in the past. It's a matter of convincing some of our partners in the financial institutions to work with us."

Schmalz says more aggressive lending policies are needed to help fuel the gaming industry. He's confident that as e-commerce and digital media become bigger industries, lending models will adapt and evolve over the next decade or two. But that shift could take longer in Canada than in the U.S., and that will put Canada's gaming industry behind the eight ball. "The worry I have is that Canada, because of its conservative nature, is going to hamstring our industry. Right now the tax credits are really the only thing that gives us our advantage."

Caouette adds that EDC's Accounts Receivable Insurance may also be helpful to the industry by protecting developers from non-payment by their distributor in foreign markets. The insurance increases margins on receivables to improve liquidity and availability in banks.

When meeting with Canadian video game companies and foreign buyers during the last several months, Caouette has noticed a consistent reaction: none of them were aware of EDC or what it can do. "It became clear that there is value EDC can bring. Most are amazed our ability to support the industry exists." Awareness about EDC's offerings is now growing slowly but surely, with Caouette attending several recent game developer conferences.

He says the demand for equity or debt funding is much higher than actual supply and that is where EDC is trying to change things. EDC now has a video game industry penetration rate of 5 to 10 per cent, something Caouette is working hard to boost.

In addition to increasing its presence in the video gaming industry, EDC will move into e-learning, special effects and animation, and other sub-sectors that continue to be dominated by software and IP, Caouette says.

Meanwhile, gaming industry players are welcoming EDC's increased involvement in the industry. Schmalz, who has been in discussion with EDC recently, notes "they're wading into the industry in small but meaningful steps." EDC could have much to offer, particularly for smaller developers, he says.

Activision's Ward adds that even if his company doesn't make use of EDC services, "by funding and helping build the infrastructure among the independent developers in Canada, they are helping us indirectly." And Kelso notes that "the more independently you can finance, definitely the more liberties you have with publishers." ■

CLICK . . .

- **rcaouette@edc.ca**
- **digitalextremes.com**
- **interactiveontario.com**

Made in Canada!

Entertainment Software Association has released a list of new made-in-Canada games showcased in June at E3 2010 – the preeminent trade show for the video gaming industry. More than 20 major made-in-Canada games were showcased by software association member companies for the first time at this year's show in Los Angeles.

- Assassin's Creed Brotherhood (Ubisoft)
- Assassin's Creed: Lost Legacy for the Nintendo 3DS (Ubisoft)
- Battle of Giants: Dinosaur Strike for the Nintendo 3DS (Ubisoft Quebec)
- Company of Heroes Online (Relic Entertainment/THQ)
- EA SPORTS Active 2 (EA Canada)
- FIFA Soccer 11 (EA Canada)
- Hollywood 61 (code name) for the Nintendo 3DS (Ubisoft)
- Kinect Joy Ride (Big Park/Game Studios)
- NHL 11 (EA Canada)
- NHL SLAPSHOT (EA Canada)
- NBA ELITE 11 (EA Canada)
- NBA JAM (EA Canada)
- Pirates of the Caribbean Armada of the Damned (Propaganda Games/Disney Interactive Studios)
- Scrabble for iPad (EA Mobile Montreal)
- Shaun White Skateboarding (Ubisoft)
- Shaun White Skateboarding for the Nintendo Wii (Ubisoft)
- Tetris for iPad (EA Mobile Montreal)
- Tom Clancy's Splinter Cell Chaos Theory for the Nintendo 3DS (Ubisoft)
- TRON Evolution (Propaganda Games/Disney Interactive Studios)
- Warhammer 40,000: Space Marines (Relic Entertainment/THQ)
- Your Shape Fitness Evolved for Kinect on Xbox 360 (Ubisoft)

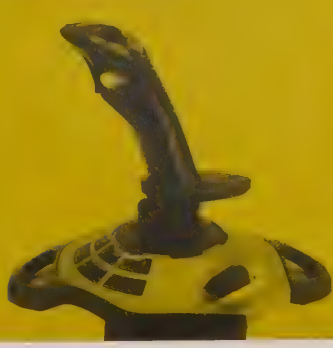
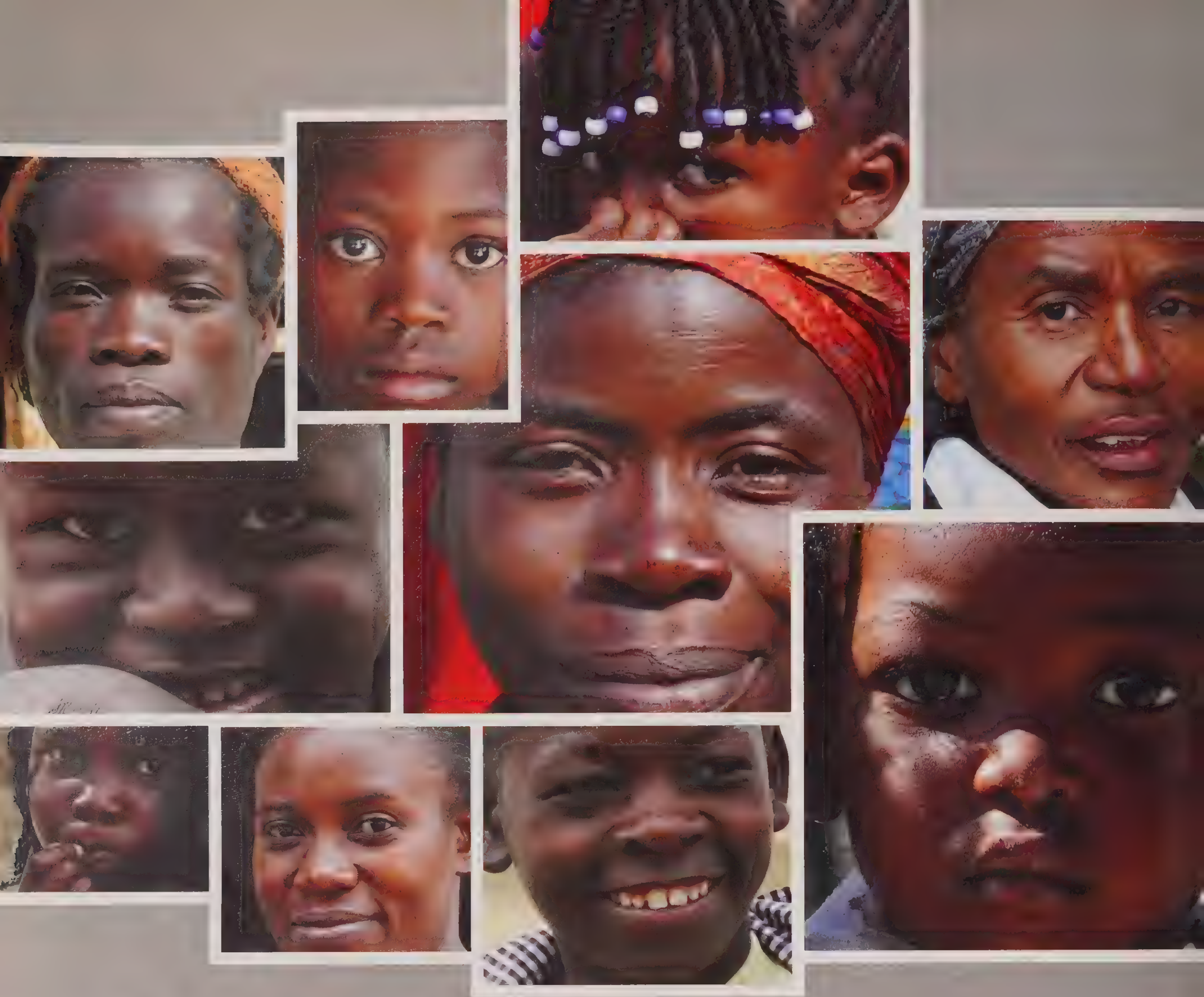


Photo: ©iStockphoto/Jerges Cortina



CARE and EDC in Zambia:

Helping Entrepreneurs Thrive

BY TS BUCHANAN

Zambia's agricultural communities face serious challenges – from drought, disease and isolation, to a lack of awareness of new products and technologies. But through a partnership with CARE Canada, EDC is helping to bridge the gap in this critical element of Zambia's economy.

"Often, a simple matter of the right seed and fertilizer can greatly impact a farmer's ability to make a living, such as a hybrid maize seed that is resistant to drought and common diseases," says EDC's Kate Parker, who is currently in Zambia lending her expertise to an agricultural small-business development project as part of EDC's global community investment partnership with CARE Canada. But first, Parker notes, farmers need to be made aware of these products and technologies – and to be able to access them.

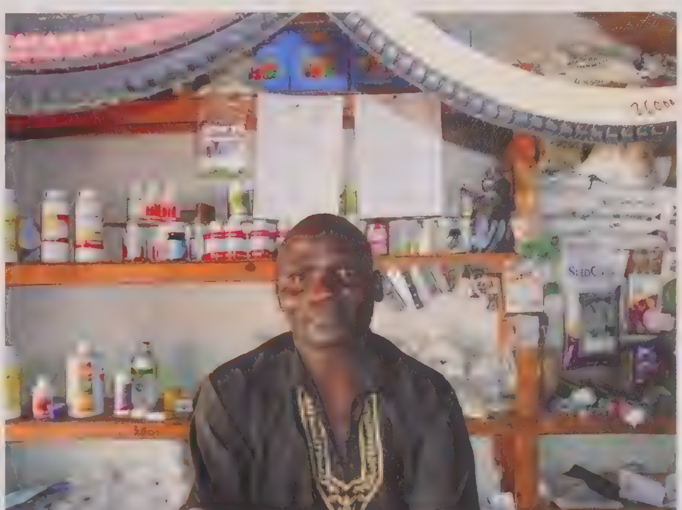
Agriculture represents about 40 per cent of Zambia's GDP, so it's no surprise that it's one of the focal points for CARE's programming in the country. Although 60 per cent of the land has high potential for agriculture, only 15 per cent of arable land is currently being cultivated. Smallholder agriculture dominates the rural economy and provides livelihoods for about one million households. Commercializing this agriculture is an important element in Zambia's strategy to increase economic growth.

However, most smallholder farms in Zambia are located in very remote locations, making them particularly vulnerable to external shocks such as prolonged droughts and floods. Often more than 200 kilometres from the nearest depot, many of these farmers have little or no access to pesticides, fertilizer or modern irrigation techniques. The soil is generally overused and it's difficult to get medication for sick livestock.

In fact, many of these small households are so isolated they aren't even aware that better inputs and technologies exist, and have relied on traditional farming methods for generations. For example, most farmers use recycled maize seeds, which produce much smaller yields, are prone to disease and require a great deal of water to grow.

Under these circumstances, a variety of strategies are needed to help Zambia reach its agricultural potential, says CARE Country Director Mark Vander Vort. "Our programs are designed to help these people build an asset base that will enable them to cope with external shocks."

To this end, CARE's ADAPT program is training local agro-dealers in remote communities to serve as middlemen between farmers and large suppliers of inputs. Dealers buy from suppliers, stock the inventory locally, resell to farmers in remote areas and advise them on more effective farming techniques.



CARE's ADAPT program trains agro-dealers like Perry Zulu who serve remote farming communities.

EDC's Parker is putting her small business development expertise to work coaching these agro-dealers on business management skills.

"One of the biggest challenges for the agro-dealers right now is cash flow," says Parker. "Currently, they have to pay their suppliers in full, up front, but often the dealers don't have enough cash on hand to buy the inventory."

To address this challenge, she is working on a supplier guarantee program to help dealers access credit, and on building relationships between dealers and suppliers. CARE also provides startup capital on a matching grant basis.

Parker is also advising the agro-dealers on marketing and promotional techniques. "Obviously the business challenges they face here in Zambia are not what I'm used to dealing with in North America," she says. "Their customers don't have Internet access, televisions or cell phones, so marketing can be tricky. They have to travel long distances to visit their customers, sometimes 30 kilometres, but they do it by bicycle.

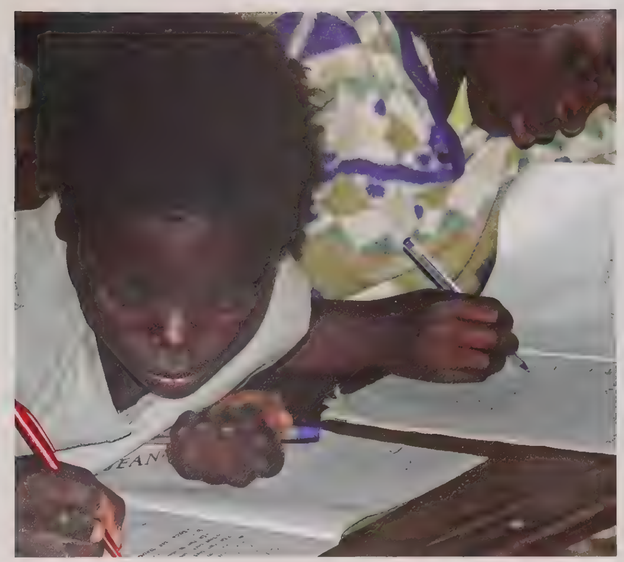
"I'm dealing with people who have the equivalent of $20 to invest in business development, so it's been a bit of an adjustment," says Parker, who is used to dealing with EDC's large transportation clients. "But I've learned that basic business concepts apply no matter where you are.

"Living in these remote communities, these people have a lot working against them, but they're highly motivated," she observes. "I've seen an amazing amount of ingenuity and entrepreneurial spirit." Some dealers have introduced customer loyalty programs, produce flyers, and build portable kiosks for local markets. "Most of these dealers are pretty savvy people," she adds. "They just need a few basic skills to grow their business."

"Soon, I plan to open more outlets in even more remote areas," says agro-dealer Perry Zulu, with whom Parker met during an extensive trip throughout the country's Copperbelt region. Parker notes that visiting Zulu was not a typical business trip. After traveling four hours of dirt road, she hiked through a kilometre of bush to meet with this particularly enthusiastic agro-dealer.

"With the business training and small grants I get from CARE, now I have the confidence and the knowledge," says Zulu. "Working with CARE has also helped me grow my customers." CARE sponsors day-long demonstration events, where farmers can come and view the different products of the large suppliers. "Getting all these farmers together gives me a chance to talk to them, one on one, and build a relationship."

To help dealers to sustain the benefits of ADAPT, this program is also working towards building a national association of agro-dealers and suppliers, encouraging them to work together,



CARE Zambia is training teachers, providing school supplies and improving school infrastructure.

negotiate fair prices, resolve packaging issues, mentor each other and advocate for agricultural policy changes with the Ministry of Agriculture.

To date, CARE has trained 500 agro-dealers throughout the country and when it concludes in 2011, ADAPT will have established 650 agro-dealers servicing more than 90,000 remote rural farming households.

"Ultimately, our overarching mandate is to help reduce poverty," says Vander Vort. "We work on promoting economic growth and enhancing private-sector competitiveness, but for these efforts to have an impact we also need to help raise the quality of basic education, reduce the incidence of HIV/AIDS and advocate for better governance.

"And all of our work, whether agricultural development or urban water sanitation projects, we try to do in a sustainable manner – build the local capacity to maintain these activities when the project ends, so we incorporate training in basic business concepts into most projects as well," he adds.

CARE has had a presence in Zambia since 1992 when it was invited by the Zambian Government to come and help during a devastating drought. Since that time, its presence has grown considerably and it now has about 220 staff in nine field offices throughout the country as well as satellite offices in some of the more remote regions. In 2009, CARE Zambia's work helped more than 500,000 people. ■

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Communicating CARE's impact

BY TS BUCHANAN

I joined CARE Zambia in May to help communicate its activities in the region. While CARE has a head office in Lusaka, its projects are scattered across a wide range of remote locations, touching virtually every corner of Zambia. For this reason, sharing information about what works well and what the projects are achieving is essential for long-term success.

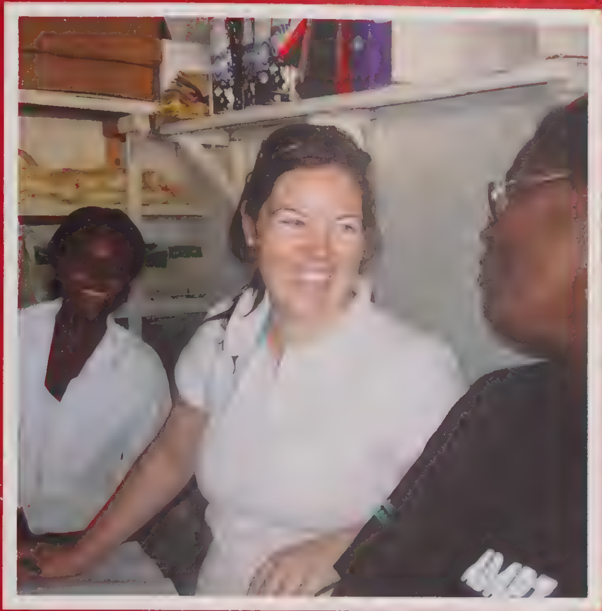
After two decades in Zambia, CARE has amassed a great deal of experience, so many of the projects are based on previous, successful models. My role is to make sure that the work being done is well-documented in various media: reports for donors, learning products for internal staff, success stories for fundraising campaigns. I'm also creating a library of images, because you can't really tell the story of CARE's work without putting faces to the people who benefit from it.

These stories are also an important part of CARE Canada's efforts to help its strategic partners and donors understand the huge difference their contributions are making by empowering Zambians to overcome chronic poverty. I'm also helping to recognize the contributions made by many of the individuals working on the projects, many of whom are volunteers. These are the people who have impressed me the most – the teachers and caregivers – all volunteers who do the work simply for the benefit of their communities.

For example, an estimated 1.1 million children are orphans as a result of HIV/AIDS. In Zambia, it all comes back to the "unholy trinity" of food insecurity, HIV/AIDS and poverty, says Country Director Mark Vander Vort. "These three challenges exacerbate each other, so you can't significantly reduce the impact of one, without dealing with all three in some way. Beyond economic help, these communities also need educational and health mechanisms to help them cope."

CARE Zambia is working to lessen the impact of HIV/AIDS on orphans and vulnerable children in poorly served communities by training volunteer teachers and caregivers to better meet the needs of these children. They train the teachers in better teaching methods, supply the school with textbooks, desks and furniture and take care of some basic infrastructure needs like running water and sanitation. Since this project began, CARE has trained 350 community caregivers and 150 teachers throughout the country, for the benefit of 80,000 children.

Many of CARE's projects rely on this growing network of volunteer caregivers to provide critical services directly to the communities in which they live. I've met many of them and they're pretty amazing women. CARE likes to call them the Agents of Change.



EDC's Kate Parker is in Zambia to help local agro-dealers develop their business management skills.

Beyond Exports

In 2009, EDC began a four-year partnership with CARE Canada, *Beyond Exports*, which aligns EDC's community investment with the emerging markets in which our customers work, and sends EDC experts for temporary assignments on CARE projects.

EDC's TS Buchanan and Kate Parker joined CARE Zambia's team from May to September 2010. Parker leant her expertise in an agricultural, small-business development project, while Buchanan worked on CARE Zambia's communications needs.

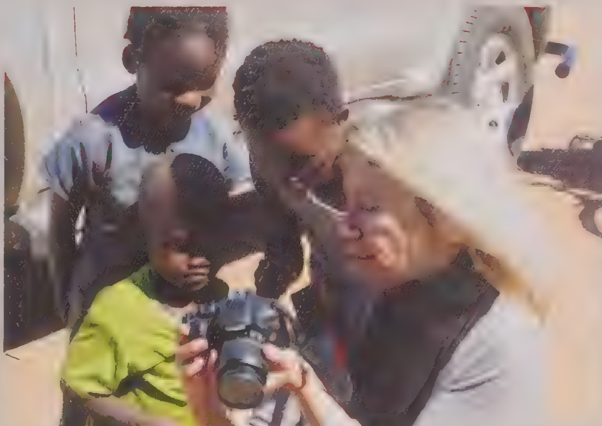
Also this year, two EDC employees joined CARE Canada's Canadian head office team to contribute to the organization's research and analysis. In 2009, two of EDC's small business advisors spent four months working on CARE projects in Peru.

Zambia is one of the most politically stable countries in southern Africa and is open for business and foreign investment. Its population of 12 million people includes a growing middle class while 64 per cent of the population is located in rural areas. Chronic poverty – affecting 60 per cent of the population – is a major development challenge, as is the prevalence of HIV/AIDS affecting an estimated 16 per cent.

Theresa Malinga is a retired teacher who volunteers most of her time at a community school in Chawama. The school has 750 students and she knows most of them by name. Malinga is almost 70 years old, which is unusual in Zambia, where the life expectancy is about 40.

When I visited the school, I was struck by how little they had, at least by Western standards, but how proud they were of what they had accomplished with CARE's help. "When we started the school, we took over an abandoned building and the children sat on the floor – we had nothing," says Malinga. "But because of CARE, we have a roof, windows, desks and running water. We have a computer for the teachers and textbooks for the children. Now – it's a school."

"Many of these little ones were traumatized when they first came here," Malinga adds. Most of the children have lost parents to AIDS and are HIV positive themselves. It was unsettling for me to see all these little faces; trying to grasp what they been through and what lies ahead. But I was particularly struck by how life goes on. They played, laughed and hammed for the camera like any children would. "Now they can get support and an education," says Malinga. "Now, they have some hope for the future."



EDC volunteer TS Buchanan with local children outside an agro-dealer's shop in Zambia's Mumbwa District, north east of Lusaka.

Rail Trade Back on Track

Foreign sales growing for Canada's rail industry

BY DENNIS AND SANDI JONES

With the driving of the Last Spike in 1885, Canada's transcontinental railway was transformed from dream to reality. Despite avalanches, floods, blizzards, political upheavals and financial scandals, its builders had succeeded in pushing the rails to the shores of the Pacific. Given 10 years to complete the line, they finished it in only five, and in doing so ensured that British Columbia would become part of Canada.

The new railway did more than unify the country. Building it also shaped the future of Canada's railway industry, which today remains a vital contributor to Canadian economic strength and is recognized worldwide for its expertise in train-to-track manufacturing and development.

"We have more than 400 rail and transit companies, employing more than 60,000 Canadians," says Jay Nordenstrom, Executive Director of the Canadian Association of Railway Suppliers (CARS). "They do about $4 billion worth of business within Canada annually, but foreign sales are critical to our sector and are growing very rapidly. Our exports are about $5 billion every year and about 80 per cent of CARS members are doing business abroad. Even the companies that haven't traditionally been exporters are looking at high-growth foreign markets, not merely as a strategic investment but as a necessity."

When estimating the size of the sector, CARS doesn't include suppliers of basic materials, such as steel makers. But even without these companies, the supply chain is highly complex – it provides not only finished locomotives, freight cars, passenger cars and track equipment, but also the components to make them. Also within the supply chain are the engineering, design and other consulting services that make up the non-hardware side of the industry.

One characteristic of the supply chain, relative to some other sectors, is its fragmentation. "Not much consolidation is taking place within the industry," observes Mike Brownhill, EDC Sector Advisor, Transportation. "That's partly because rail equipment production, on a unit basis, is not a high-volume industry, even though its assets are large. It is also very cyclical; rail car sales spike up and down, for example, and businesses have to cope with those cycles. As a result, companies that want to survive as rail-supply firms have to be very diverse."

A chain of diversity

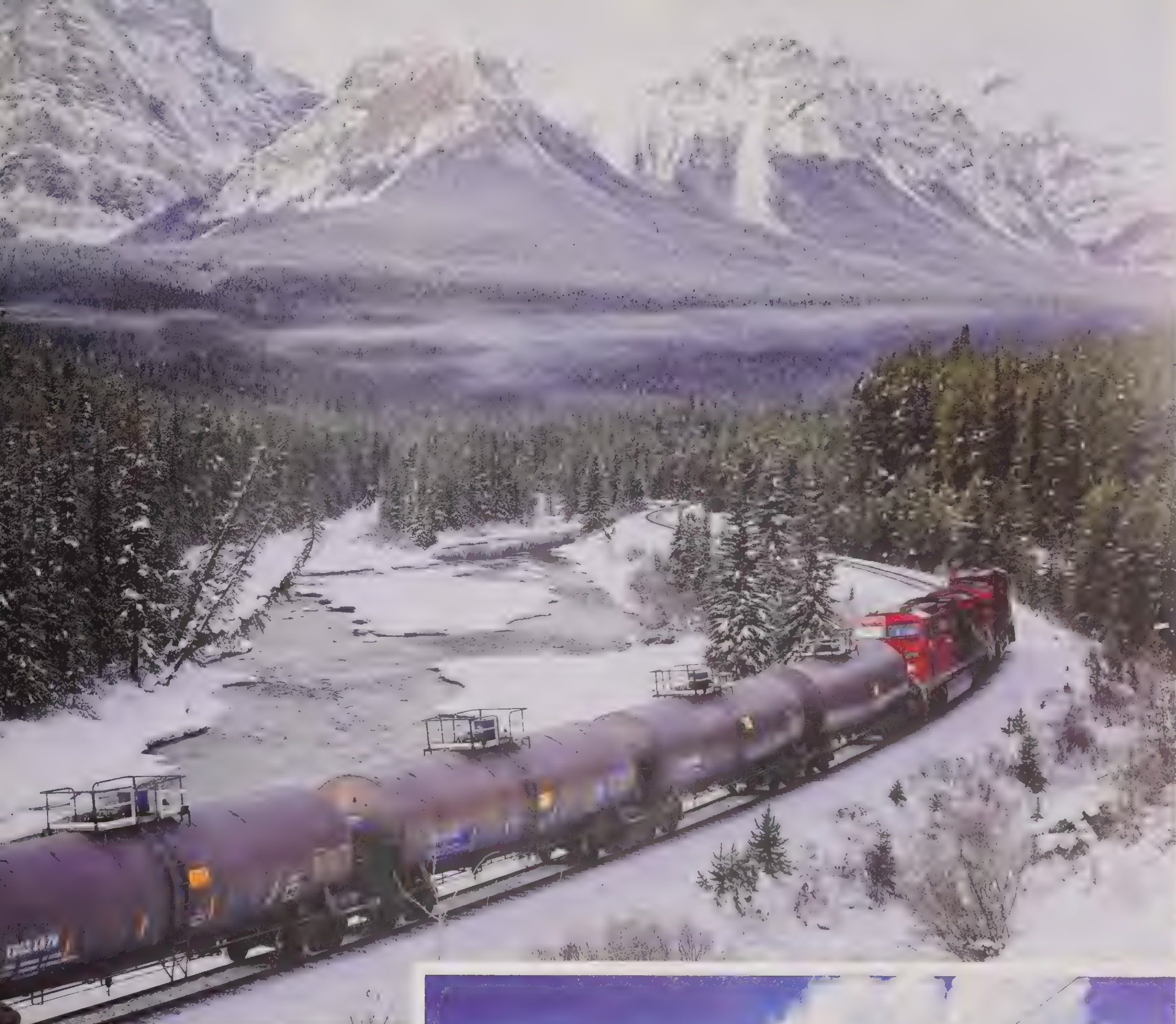
On the positive side, the industry's diversity is one reason for its resilience and importance in the Canadian economic landscape. This diversity is reflected in the industry's outstanding ability to construct railways through any terrain from deserts to mountains, and for any weather from tropical monsoons to arctic winters.

"I would say that this adaptability is our biggest single advantage," says Nordenstrom. "Because our market has historically consisted of a few major buyers and a large number of small but diversified suppliers, we've been forced to be very competitive, innovative and efficient. As a result, we've developed rail technologies that can deal with the harshest conditions; added to that, the sheer size of the country has made us experts in long-haul rail freight. The world recognizes those abilities, so we regularly see foreign delegations coming to Canada to learn how we move goods and people across very difficult terrain, quickly and efficiently."

Canada's rail industry is able to construct railways through any terrain from deserts to mountains, and for any weather from tropical monsoons to arctic winters.

Canadian rail companies also have an excellent record for after-market service abroad. "Our foreign customers know we're there for the long term," says Nordenstrom, "and the relationships we've built in those countries have created our international reputation. That helps Canadian companies that are already exporting, and it does a big favour for Canadian businesses that are trying to get into international markets for the first time – our reputation precedes them."

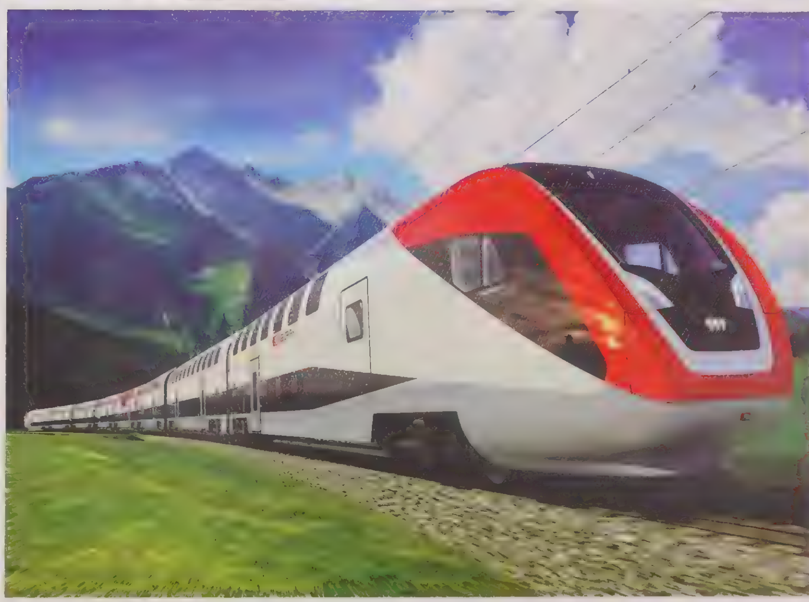
Innovation is key to the industry's competitiveness abroad. One important area of Canadian leadership is the development of positive train control (PTC)



systems, which use technology such as digital data links, continuous positioning systems and onboard computers to monitor and manage train movements for increased safety.

Signal successes

Over the years, this combination of expertise, innovation and service has produced many successes for the industry and for the companies that have also tapped into EDC's financing, insurance and bonding services to grow faster and farther. Electro-Motive Diesel (EMD), whose final assembly plant is in London, Ontario, is now the world's largest builder of diesel-electric locomotives for all types of commercial railroad operations. It has an enormous international presence, from Argentina to Zimbabwe, and provides not only equipment but also ancillary services such as locomotive maintenance and PTC systems.



In June, 2010, Bombardier announced an order from SBB for 59 TWINDEXX Double-deck Inter-city Trains in Switzerland.

Then, of course, there's Bombardier, the flagship Canadian company that builds state-of-the-art aircraft and trains. Bombardier Transport, the company's rail division, is based in Berlin but remains very much a Canadian company whose supply chain uses a good deal of equipment from Canadian suppliers.

A major Bombardier success for 2010 is a US$1.6 billion contract with Swiss Federal Railways (SBB) to build 59 double-deck, long-distance TWINDEXX trains consisting of 436 air-conditioned carriages. This is the largest vehicle order in SBB's history, and Bombardier outbid two major European manufacturers, Siemens Switzerland Ltd. and Stadler Bussnang AG, to secure the contract. Close on the heels of that achievement came another important Bombardier sale, an order for 74 MOVIA transit cars from the Delhi Metro Rail Corporation in India. Bombardier continues to deepen its roots in emerging markets such as China, India and Mexico.

At your service

The services and consulting side of the sector is highly successful as well, and capitalizes on the long Canadian experience with designing and developing rail systems that can go anywhere and carry anything.

CPCS is a major presence in this segment of the industry. Based in Ottawa, the firm provides specialized infrastructure development services to international clients, and has a history of involvement in rail and urban transit projects around the world. "As with all our sectors of interest," says Carolyn Mackenzie, CPCS's Vice President for Marketing, "our primary work with rail is at the front end, in the areas of planning, project feasibility, public-private partnerships and transaction structuring. At least 90 per cent of what we do is outside North America, much of it in emerging markets, including significant work in Africa, and we're increasingly active in the Middle East."

Jordan is currently a key focus for CPCS, says Mackenzie. "We're working on a brand new railway the Jordanians want to build, and we're getting ready to go to the market for final design, construction and operating contracts. This is a huge project that will cost around $4 billion, and it has major strategic implications for the region – the Saudis, next door to Jordan, have two very large railway developments underway, one of which would connect the proposed Jordanian network to the Gulf States.

"EDC's help is crucial when we're trying to put together complex international deals," says CARS' Jay Nordenstrom.

"This is all part of a regional plan for railway development, with Jordan as a link to Syria and Turkey, and onward to Europe. That's the long-term plan, so the Jordanian project is of great strategic importance."

Jordan doesn't have the oil wealth of some of its neighbours, so financing such a huge project is a challenge. This is where CPCS plays a vital role, says Mackenzie. "The Jordanian government intends to establish a company to finance and build the actual rail infrastructure, and we're now finalizing the procurement strategy for doing that. We'll also be looking for a private operator for the new railway. This would be a public-private partnership in which the operator would have a long-term concession of 30 years to run the system, while the government would continue to own the railway infrastructure."

Recession and response

Successes notwithstanding, the effects of the global economic downturn have been brutal for some Canadian firms in the sector. The freight-related manufacturers suffered especially badly; in consequence, many of these companies are turning to international markets or trying to diversify by adapting their products and technologies to other subsectors, such as transit.

"Our original equipment manufacturers (OEMs), especially in rail cars, have been hit hard," says Nordenstrom. "With the downturn, thousands of cars in North America were simply parked on sidings, and that situation also affected the OEMs' sub-suppliers as the orders dried up. The same applies to locomotives. It's been tough, but we're seeing a bit of a rebound now, and we believe that companies like EMD are poised to do very well."

Conversely, a number of track specialists have actually seen business go up, since rail operators like to upgrade and maintain their tracks when traffic is slack. Similarly, some component makers have kept much of their market because operators are choosing to repair their rolling stock rather than replace it.

"Still, equipment eventually wears out, and changes in commodity shipments demand new types of rail cars," says EDC's Brownhill. "Consequently, I think that international and domestic demand will both come back, and the economic stimulus packages brought in by various governments can provide opportunities for companies to capitalize on the rail infrastructure needs of many countries.

"Another likely area of growth is on the operating side; many emerging markets have brought in stimulus funding to acquire rail infrastructure and equipment, but they still need to develop the skill sets required to operate their systems efficiently. Building a new short-haul mining railway, for example, won't pay off over the long term unless its operators know about things such as maintenance and systems management."

Given the reach and nature of its business, a company like CPCS is well positioned to observe the competitive environment from the development and planning perspective. And it's *very* competitive, according to Mackenzie. "Oman, one of the Gulf States, just put

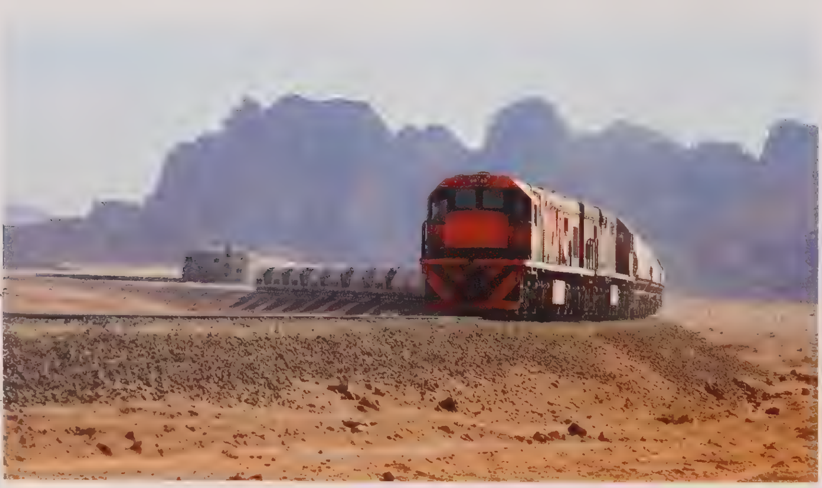


Photo: ©iStockphoto/Adrian Beesley

Amman to Zarqa light rail system in Jordan.

Photo: ©iStockphoto/Fontmonster

Canada's rail sector

400 rail & transit companies

60,000 employed

$5 billion annual exports

out a tender for design services for a planned railway, and there were more than 30 expressions of interest from major international infrastructure firms. The European companies are always active in these markets, of course, but the Chinese and South Koreans are increasingly present, and these relative newcomers can provide strong competition for Canadian firms that provide engineering design services."

Strategies for success

Besides diversification and the pursuit of foreign sales, other key strategies can sharpen a company's competitive edge. The market is highly price sensitive, so a company that can include financing as part of a deal will have an advantage over a business that can't. Providing turnkey solutions to cover a customer's needs from beginning to end of a project is another strong selling point – one for which the Canadian industry is already known. Finally, working with industry associations such as CARS and partnering with Canadian governments can help broaden the sector's business development network and help them learn about new opportunities.

Huge rail projects are underway or being planned in many parts of the world, but the priority markets for Canada are likely to be the Middle East, India, China and some other emerging economies, as well as the United States, where high-speed rail is a priority for the Obama administration. In Africa, Ghana is planning major projects, and Canadian firms have already been successful in places such as Mozambique, Nigeria and Algeria.

"The Middle East is a burgeoning market," reiterates Mackenzie. "There's a real push in the region to develop rail networks where none now exist, and clients there are very interested in taking advantage of Canada's experience with building and operating railways. This is especially true of the Gulf States, where rail projects are moving forward at a very rapid pace as these economies try to diversify in anticipation of a post-oil world. They're looking to Canada for expertise that is quite different from that of our European competitors. Those firms concentrate on short-haul applications, compared to Canada, and are focused more on passengers than on freight."

For CPCS, sub-Saharan Africa is another rich source of business, and the company is currently working on projects in Kenya and Nigeria. These are now at the development and planning stage, but eventually will need locomotives, rolling stock, tracks, control systems, switches and signalling equipment, and the training that will make everything work. Among the other African countries with projects in hand are Uganda, Tanzania and Botswana.

Another area of opportunity is industry-specific rail development, particularly for the mining sector. Many Canadian engineering firms have clients who are operating mines abroad, and railways are usually the method of choice for transporting thousands of tons of ores or minerals. If a mine is being developed somewhere, you can be sure that a railway will be close behind.

The role of EDC

Canada's rail industry sees EDC as a vital support for its members abroad. "Many of our companies work closely and successfully with EDC on a number of fronts," says Nordenstrom. "EDC's help is crucial when we're trying to put together complex international deals, and our need for services like that is only going to increase. We want to continue strengthening that relationship, especially so we can take on higher-risk projects in emerging markets, which is where we see our best opportunities."

CPCS has a similar story, according to Mackenzie. "Most of our customers are overseas, so we use EDC's Accounts Receivable Insurance (ARI) to guarantee that we'll receive payment even if a buyer defaults. That gives our banks some extra comfort when we need financing; because EDC is there for us, they know we'll always get paid and so will they. We're also becoming more creative in using other EDC products when we're developing international projects, such as obtaining loan guarantees for commercial banks to reduce the interest rates for our clients. EDC also allows us to offer our clients a package of services that includes financing. In one of our projects in Angola, for example, EDC guaranteed a commercial bank loan for the financing package that will enable the Angolan government to purchase our services."

As well as ARI and loan guarantees, EDC provides bonding support for operators and service providers, and working capital support for OEMs and other companies, depending on need. And, in key markets such as Saudi Arabia and the Gulf States, EDC has full-time representatives who can help Canadian companies develop local networks and conclude local deals.

The Canadian rail industry has recently endured one of the worst economic downturns of the past 100 years, and for the most part has survived intact, if occasionally battered. But as more and more countries come to understand the inherent utility and efficiency of rail transport, there may well be a railway renaissance on the horizon. "We see our industry as a large, dynamic and growing community," says Nordenstrom, "and a vital part of our economy and manufacturing sector. So I see long-term growth ahead, built on a solid foundation of Canadian system design, technological expertise and our ability to compete for rail projects around the world – and win them." ■

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› **cpcstrans.com**

7 Essentials of Commercial Contracts

BY BRUCE GILLESPIE

1 THE BASICS

The terms and conditions in a commercial contract should be written as clearly and unambiguously as possible to avoid any potential confusion, then signed and dated by both parties. Any changes to the original contract should also be agreed to in writing through a formal amendment that is signed and dated by both parties. If external financing is required, the contract should include a clause that such arrangements must be in place and in force before the contract becomes valid.

A contract should clearly identify all of the parties involved by their full, legal names, not their trade names. It should also contain a clear description of the nature of the transaction being conducted – in other words, a detailed explanation of the goods or services being sold, as well as who is buying them and who is exporting them.

It should also include a statement of obligation that outlines the scope of the exporter's responsibilities, such as whether the agreement includes only the sale of a good or service or its installation, related training, etc., as well.

2 PERFORMANCE INSTRUMENTS

A commercial transaction may require the exporter to issue performance instruments – such as bank letters of guarantee or letters of credit or surety bonds, collectively referred to as bonds – to secure its performance obligations. If this is the case, the contract should contain a clause that explains the financial obligations covered by such instruments, outlining:

- when the bond will be issued and for what purpose;
- what will trigger the bond's expiry; and
- whether there are mechanisms in place to increase or decrease the amount of the bond.

It is important that the performance instrument corresponds to and reflects the requirements of the contract. For example, the starting and ending dates should match those outlined in the contract, detailing when the bonds are issued and when they expire.

3 PAYMENT ARRANGEMENTS

A contract should clearly set out the total payment details negotiated between the exporter and the customer. It should also state whether the price is fixed or adjustable and stipulate the currency in which the payment is to be made.

The contract should also outline the payment terms. For example, will the exporter be paid in full upon the delivery of goods and/or completion of a service, or in installments at pre-determined milestones? The contract should also include information on whether there are any contract obligations that would suspend payment and how the exporter will be paid – i.e., via an irrevocable letter of credit, an open account or some sort of outside financing.

4 TERMS OF DELIVERY

The contract should stipulate how and when the delivery of the contracted goods or services will take place. That includes outlining which party is responsible for shipping costs and any damages or losses during shipment, as well as when the title to the goods will be transferred.

When writing a contract, the exporter should ensure that the delivery schedule is realistic in terms of timing and consistent with the company's capabilities and work schedule to avoid paying late penalties.

There's an old saying in business that is as true as it is frustrating: the most important clause in any contract is the one you forget to include.

Many small and medium-sized exporters have had to learn this the hard way, particularly when expanding their business to new markets around the world. That's why EDC has created a Commercial Contract Terms reference guide to help exporters avoid potential misunderstandings and disputes from the outset.

"The lending, insurance and bonding we do is all based on contracts, and often we're asked to support contracts that have flaws in them," says Mike Neals, EDC's Vice-president of Marketing. "So, we'll have to ask the customer to go back to their buyer and try to renegotiate. Sometimes they're fixable, but sometimes contracts are signed that we can't suppo[rt] because they put the exporter at undue risk."

That's why EDC developed its 12-page guide on key t[erms and] conditions that should be included in commercial contracts. The c[omplete] guide is available for download from the EDC website at ed[c.ca...] here is an overview of some of its highlights that exporters [should] consider when writing contracts.

Keep in mind that the guide and this article are for informatio[n pur]poses only. They are not intended to provide legal advice and shou[ld not] be taken as such. EDC customers should exercise due diligence in dra[fting] contracts and should seek out professional legal advice in preparing t[hem.]

5 PENALTIES AND LIQUIDATED DAMAGES

The penalties and liquidated damages clause identifies the exporter's obligations in the event that it does not comply with some of the contracted obligations. This clause should address the following points:

- Are the penalties for late delivery reasonable with respect to the value of the goods and the damages the buyer might incur as a result of late delivery? Penalties are normally calculated as a percentage of the contract price or value of the delayed goods or services for a specified period of time.
- Can the penalties be deducted from any payments owed to the exporter?
- Can the customer call the exporter's letter of guarantee or bond to obtain penalty payments?

A contract should also include a force majeure clause that lists the types of events both parties agree will cause an excusable or justifiable delay in the exporter's or the customer's obligations and/or cancel the contract altogether.

6 DISPUTES AND RESOLUTIONS

A strong contract should outline the agreed process for settling disputes, including the potential for arbitration. Dispute resolution through an arbitration process – typically subject to international law – where disputes can be settled by independent third parties is often preferable to resolution through the courts of the customer's country.

A contract should also stipulate the rules, location and language of arbitration, as well as which party will pay for the associated costs, and whether the arbitrator's decision can be appealed to the courts.

7 BOYCOTT CLAUSE

The Canadian government's policy on international economic boycotts restricts support and assistance for exporters who have agreed to contracts containing boycott provisions. As such, to be eligible for EDC support, exporters must ensure their contracts do not contain any boycott provisions, which generally engage in discrimination based on national or ethnic origin, race or religion, or require the exporter to refuse to purchase or sell goods and services to a particular country.

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ALUMA SYSTEMS

Diversification into emerging market spurs growth

BY SHELDON GORDON

Aluma Systems' concrete construction division is known around the world for improving the quality and speed of construction. A key supplier of construction equipment for domestic and foreign contractors in more than 50 countries, Aluma has 350 employees and some $150 million in annual revenues – 30 per cent of which is generated overseas.

The Concord, Ontario company's products are used in projects ranging from high-rise towers and dams to stadiums, bridges and transit systems. Its relationship with EDC began three years ago when Aluma was involved in a project in Romania where the client would not provide a secure payment. "We insured the receivable through EDC," says Sol Solomou, Director and General Manager, International.

EDC export credit insurance soon covered Aluma deals in other countries. Though none of its customers has defaulted, Solomou says the insurance has been very valuable, especially to the company's shareholders. "They're reassured, and give us more freedom to expand the business without requiring costly secure payment from clients," says Solomou. Aluma and EDC now are discussing opportunities for trade finance, and the company's growing stable of overseas projects is likely to deepen its ties with EDC.

Owned by a group of private investors since 2007, the company had its origins as a unit within Toronto condominium developer Tridel Corporation. Struggling with rising labour costs in the early 1970s, Tridel launched a construction technology division. The result was the Aluma Beam, an innovation in construction engineering that revolutionized the industry by introducing high-grade aluminum forming and shoring components to replace expensive and heavy steel equipment.

By 1975, as other contractors sought these products too, Tridel spun off Aluma into a wholly-owned subsidiary. The contractor that built the Olympic Village in Montreal in 1976 was one of the first to use the Aluma Beam and Truss system. This involved using flying form tables, a system of formwork or moulds to make flat slabs, which boosted productivity.

Aluma first sold internationally to Venezuela and Norway in 1977, then expanded exports rapidly. By 2003, the company faced a dilemma: "It was clear that unless we were prepared to set up operations overseas and employ local people, we might as well shut down," says Solomou.

"We had been exporting directly from Canada. But it's only when you're in a country 'on the ground' that you gain a full understanding of where there is business to be had – not just the large projects, for which there is enormous competition, but also medium and small projects."

So Aluma established subsidiaries in Riga, Dubai, Mexico City and Bangkok, each becoming a hub for sales offices in, respectively, Eastern Europe, the Middle East, Latin America and Southeast Asia. The local presence paid off, and sales climbed an average of 15 per cent annually during the decade.

Then came the 2008–09 downturn. The U.S., where Aluma has eight offices, declined from 45 to 30 per cent of "domestic" revenues. Activities in Mexico also slumped, followed by sales in the Middle East, Aluma's largest market abroad, which declined following the financial crisis in Dubai.

But the Southeast Asia market stayed strong, and Aluma has been bringing equipment from the U.S. to serve Indonesia, Malaysia, Singapore and Thailand. It has also moved equipment to Mexico, which recovered quickly from its recession in the construction sector.

The company is particularly optimistic about Mexico and Brazil in the near and medium term. It anticipates substantial business as both countries proceed with huge plans to build low-income and social housing. Aluma has developed *EasySet*®, a new concrete product suited to the social housing sector.

Aluma has also had orders for *EasySet*® from Nigeria, while Angola and Mozambique are showing interest in launching their own social housing developments. ■

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Photo: Courtesy of Aluma

Aluma Systems has more than three decades of experience on projects ranging from bridges, hi-rise developments to civil construction projects.

CANALTA CONTROLS LTD.

Alberta company sells to most oil and gas regions of the world

BY KATHRYN YOUNG

During Canalta Controls' first forays into the international market, it learned the hard way how to ensure it got paid.

The lesson learned by the Red Deer, Alberta company, put simply: don't assume.

For example, as Canalta Vice-President Michael Clark explained, by assuming that business in Venezuela is conducted the same way as in Canada, including how payments are made, Canalta missed a crucial piece of information – that Venezuelan business has foreign currency controls.

Luckily, Canalta heard about EDC's products and services, such as accounts receivable insurance, and how they might help companies ease through their first steps on the international market.

"EDC became a critical part of being able to work in those markets securely," says Clark. "It gave us a sense of security to take on business knowing that we're not going to get hurt so badly. With the help of EDC, lessons aren't going to be quite as expensive."

The privately held company got its start in 1986 as an instrumentation and electrical contractor. Soon after, it moved into equipment repair and then evolved into manufacturing industrial control and measurement equipment in the early 1990s for the oil and gas sector. Now, with 50 full-time employees and many subcontractors, Canalta operates two main divisions.

The first division manufactures orifice fittings that measure the volumes of natural gas (or other gases such as CO_2) passing through a pipeline. Although the technology has been around since the 1930s, Canalta's product allows the orifice plate to be removed and inspected without interrupting the flow in the line. "That's a feature that a lot of people like and it's getting a lot of international response," Clark says.

The second division produces burner management and ignition solutions for industrial heating applications.

About 30 to 40 per cent of Canalta's sales are domestic – to oil and gas companies in Alberta, northern British Columbia and southern Saskatchewan.

Canalta began developing its international markets about 10 years ago, first in the U.S., which represents more than half its international sales, and then to Mexico and Venezuela.

Now, Canalta sells to most oil and gas regions of the world, including Singapore, Indonesia, Malaysia, Thailand, Vietnam, Pakistan, Bangladesh, the Middle East, North Africa, Brazil, Bolivia, Chile, Peru, and Colombia. Canalta established an office in Buenos Aires, Argentina last fall, to further target South America, and is breaking into Russia and expanding in Brazil.

In fact, it was the international market that helped cushion Canalta during the recent economic downturn, when domestic sales slowed. "Having that international presence really did make the difference for us," says Clark.

Last fall, EDC invited Canalta to meet Brazilian oil giant Petrobras and its suppliers during a trade mission to Calgary, resulting in an order for Canalta. During a recent trip to Brazil, Canalta's business meetings included the local EDC representative who knew the local players and advised Canalta about local business culture and EDC financing options for Brazilian companies that might make it attractive to work together.

Accounts receivable insurance is still the primary EDC product Canalta uses, but Clark says they are now investigating investment finance solutions.

Canalta's growth strategy includes promoting product awareness, especially its strong custom applications, and letting potential customers know that they offer complete solutions rather than just one piece of the puzzle.

Clark's advice to companies breaking into international markets: work with EDC when you're establishing relationships, until you're comfortable in a country. "EDC allows you to begin those relationships with some degree of confidence that you're not going to get stung," he says.

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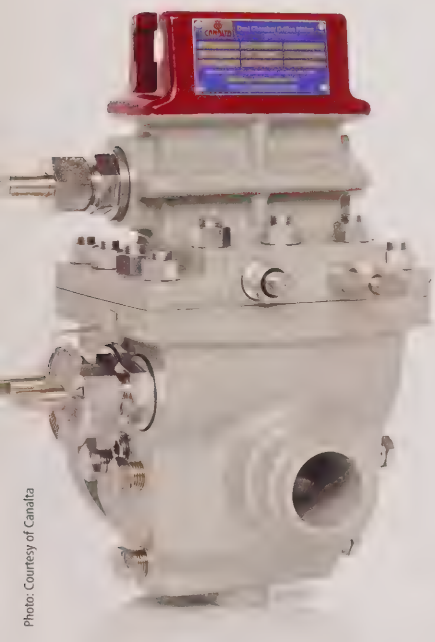

Photo: Courtesy of Canalta

The Canalta Dual Chamber Orifice Fitting.

COMMPORT COMMUNICATIONS INTERNATIONAL

Ontario-based company provides its fuel management systems to civilian and military clients worldwide

BY SHELDON GORDON

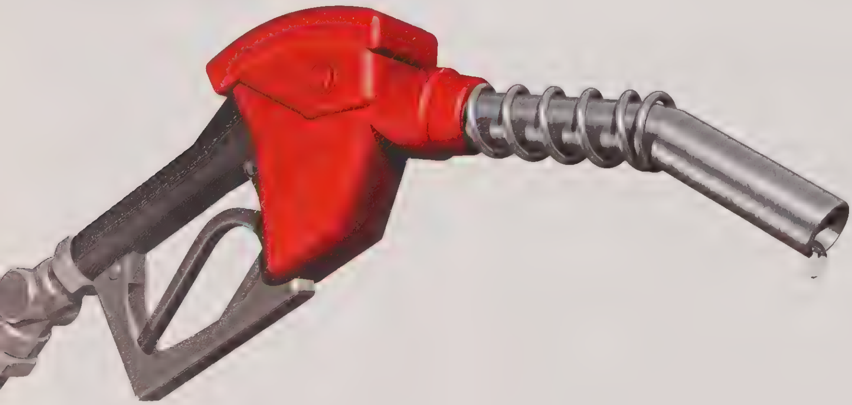

Photo: ©iStockphoto/Paul Fleet

The recession has actually been good for Commport Communications International. The company's fuel management systems, which allow customers to track the use of virtually every drop of fuel in aircraft, tanks, jeeps and trucks, are increasingly sought to reduce costs during a time of austerity.

"When fuel cost 25 cents a gallon, no one cared very much if some was lost," says founder, Chairman and CEO Dave Ralph. "But now, when aviation fuel costs $4 to $5 a gallon, if you lose 2.5 per cent of that, it's a big, big number – especially when you consider that airlines buy fuel in the billions of gallons annually."

As an example of the savings his software provides, Ralph points to the airlines operating at Newark Liberty Airport, which he says will save tens of millions of dollars through better management of their fuel inventory.

Ralph credits EDC with playing a vital role in the firm's international success. "We look to them for all kinds of advice," he says of EDC, which has provided performance bonds for Commport's contracts as well as export insurance and trade finance. "They're our export development arm."

The Aurora, Ontario-based company provides its fuel management systems to a variety of civilian and military clients around the world. Its biggest customer is the United Nations, which will rely on Commport's systems to monitor fuel use, manage inventory and plan demand for its peacekeeping missions. The company's annual revenues are growing by 40 to 45 per cent a year.

Commport is in the sixth year of a 20-year contract with the Port Authority of New York and New Jersey, the busiest airport authority in the world, to serve Newark Liberty, LaGuardia, John F. Kennedy International and its other airports. Another major customer is the Indonesian State-owned oil company Pertamina, which relies on Commport to manage fuel consumption at 54 airports around the country. On the military side, the U.S. Air Force is a major client, and Greece's armed forces have also expressed interest in Commport's services.

The privately owned company, whose annual revenues Ralph says are in the "tens of millions of dollars," started in 1988 as a provider of Electronic Data Interchange (EDI), which is the structured transmission of electronic documents between organizations that predates the Internet. Today, EDI and e-commerce services account for only 40 per cent of Commport's revenues – 60 per cent comes from its fuel management business.

"We got into fuel management through EDI in 2004–05," says Ralph. "We replaced paper-based data with electronic data in the fuel management business." The turning point came in 2006, when Commport acquired Liquid Transfer Systems (now LTS Sales), in Erie, Pennsylvania, with 35 years of experience in facilitating and monitoring the transfer of fuels and other fluids.

For future sales, Commport is looking to the Middle East and Africa. It has a pilot project under way in Abu Dhabi and is finalizing a long-term contract with Nigeria. It also hopes to add the World Food Program and other UN agencies to its client list.

One challenge the company still faces is in recruiting to bolster its software development capacity. "We can't hire staff fast enough," says Ralph. "Even in today's environment, the right employees are hard to find." The company today has 60 employees, spread between Aurora, Erie and St. John's, Newfoundland and Labrador, where it has its hardware division. ■

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PAN MARITIME

St. John's-based company diversifies into Middle East

BY KATHRYN YOUNG

Perseverance, homework, and backing from EDC enabled Pan Maritime Energy Services Inc. to expand in the Middle East oil and gas industry.

Pan Maritime's vision was to seek global markets for its project management and engineering services in the offshore oil and gas industry, but in a more aggressive and focused manner. Moya Cahill, who co-founded the St. John's-based company in 1998, brought her previous business experience in Nova Scotia, Chile and Houston to bear.

"Our biggest and perhaps riskiest move was when we decided to expand into the Middle East, to set up a branch office in Doha," says Cahill, Pan Maritime's Chair of the Board. For the first 18 months, Cahill spent significant time in Doha, Qatar to understand the players and culture and piggyback on previous relationships with Exxon Mobil, Maersk and Norsk Hydro.

"One of the Exxon Mobil guys said 'Gosh, I'm starting to see you more than my family in Houston'," Cahill explains. "I said, 'There's one way of dealing with that. Just give us a contract and I'll leave you be.'"

"Clients, particularly in foreign markets, need to see your commitment," she says. "They need to see your ability to follow up and that was certainly what we demonstrated to the team in Qatar with players like Exxon Mobil. They recognized our determination and our follow-up and our commitment and through that we got to the next stage."

Eventually, Pan Maritime won its first contract in Doha.

That was in 2005, and Pan Maritime now receives about 80 per cent of its revenue – about $12.5 million – from its Middle East operations, with additional projects in Abu Dhabi and Dubai.

"EDC was key in supporting our growth and expansion in Qatar," Cahill says. "We wouldn't have been able to pull it off without EDC. Our partners outside Canada are envious of EDC and our ability to use its services to support our success."

Pan Maritime primarily uses EDC's accounts receivable insurance, as well as bid bond guarantees, which are required for most engineering work in Doha.

A key driver for global expansion was to equalize the ups and downs of Canada's east coast market, where mega-projects come along only every four or five years.

"We were forever trying to manage the peaks and troughs. So I was looking for a steadier, stable market and that's what we found in the Middle East," Cahill says. Since its establishment in Doha, the company has peaked at about 100 employees, including placing people in Dubai, Italy and Japan.

Global diversity also helped insulate Pan Maritime from the recent economic slowdown; Qatar's emir has a goal to provide 27 per cent of the world's liquid natural gas and he protects the industry.

Cahill says anyone contemplating global expansion must do their homework.

"The Middle East isn't for everyone," she says. "It's really important that you take the necessary time to pick your partners wisely. Prepare a solid business plan and raise ample equity because I've found that establishing an operation outside Canada takes more time and more money than you think."

Photo: Courtesy of Pan Maritime

Moya Cahill, Pan Maritime's Chair of the Board.

And don't forget to include EDC in your plans. "They made our bankers here at home a lot more comfortable in supporting our line of credit," Cahill says.

Cahill is transferring that positive experience to her new-found technology company, PanGeo Subsea Inc. "We had a need, we knocked on EDC's door and once again they stepped up to the plate and are supporting PanGeo in its global expansion," she says.

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New Trade Deal Gives Canada Competitive Edge in Colombia

BY TOBY HERSCOVITCH

Canadian companies can start to ramp up their main exports to Colombia – machinery and equipment, grains and pulses, and chemicals – and much more besides. In June, Canada ratified legislation to implement a free trade agreement (FTA) with Colombia, giving it a competitive edge over the United States, which is still pondering a similar trade agreement.

Cartagena's Pier, Bolivar, Colombia.

Photo: © Oscar Garces/Age Fotostock

Colombia's Ambassador to Canada, Jaime Girón Duarte, expects tariffs and other trade barriers between our two countries will be reduced or eliminated by early 2011, once Colombia completes its own ratification formalities. "After that, I believe we'll quickly see Colombian imports of such popular Canadian products as wheat and machinery increase, displacing some imports from the United States," he says.

The FTA is one of several conditions that favour a steady pick-up in trade and investment between Canada and Colombia. Another is the fact that Colombia is overdue for massive infrastructure investments, estimated at US$20 billion over the next five years – plus some US$50 billion in oil and gas development. For example, the Colombian government has already announced plans to build a US$3.5 billion pipeline to transport oil from eastern Colombia to its Caribbean coast. "The agreement will benefit Canada's producers and exporters, reduce or eliminate tariffs on nearly all current Canadian exports, and provide a more predictable, transparent and rules-based trading environment for Canadian investors," says Peter Van Loan, Minister of International Trade.

International consulting firm CG/LA Infrastructure, which organized a conference on infrastructure earlier this year in Bogotá, estimates Colombia spends about US$106 per capita on infrastructure. That's well below Chile at US$311. In Canada, infrastructure spending reaches US$500 per person.

"Our infrastructure has to be modernized – we need to improve or build new roads, ports, airports, railroads, power grids and a metro for Bogotá," says Girón.

Such projects open exciting new possibilities for engineering-construction firms, equipment suppliers and investors. "Top Canadian engineering and construction companies are coming back to Colombia in full force," says Stephen Benoit, EDC's Chief Representative for the Andean Region. "Firms like Sandwell, SNC-Lavalin, Genivar, Dessau, AECOM and Brookfield, have either opened or reopened offices in Colombia, or set up joint ventures, over the past two years."

As well, HOK Canada, part of the global architectural design firm, was listed in ReNew Canada magazine's *50 International Infrastructure Projects 2009* for its work on the preliminary master plan for one of Colombia's main ports, Barranquilla. In the oil and gas sector, Benoit estimates that at least 20 Canadian junior companies are doing exploration.

Trade and investment reach record highs

Before the recession hit, foreign direct investment in Colombia from all countries reached an all-time high of US$10.6 billion in 2008. While this number declined during the financial turbulence of 2009, it started climbing again in the first quarter of this year. Meanwhile, investments in the country's oil and gas and mining industries have been rising 35 per cent year-over-year. Both are sectors where Canadian expertise and involvement are strong. Today, says Girón, Canada is the ninth largest investor in Colombia and there is much room for growth in line with Colombia's extractive and infrastructure needs.

Colombia is Canada's fourth largest export market in South America, with merchandise exports reaching close to US$650 million in 2009. That's less than the record US$800 million in 2008, but still higher than any previous year. EDC too has seen a steady increase in Canadian customers doing business in Colombia, now at about 180, from 100 back in 2005. Out of our $1.8 billion in business volume in Colombia over the past five years, close to 90 per cent is in the extractive and resources sectors.

Colombian exports to Canada, while more modest, continued to climb during a difficult 2009, to about US$400 million. On the trade menu: coffee, at 25 per cent of total exports, sugar and flowers, plus a diverse mix of other goods from cosmetics to chemicals. Colombia is the

second largest flower-exporting country in the world, behind only the Netherlands.

This steady growth in twoway trade can be traced back to 2002. That's when Colombia's then newly elected government, under [former] President Alvaro Uribe Vélez, started working hard to effect a dramatic shift in security in the country.

"Colombia was on the verge of becoming a failed state," says Girón. "We needed to regain security and a new measure of democracy to rebuild, grow and develop. We had to recover the trust of Colombians and the international community."

Through the government's peace negotiations with the country's paramilitary organizations, some 35,000 members voluntarily demobilized. While no formal negotiations took place with guerilla factions, the government estimates that up to 20,000 of their forces have also demobilized.

Girón adds that back in 2002, 565 – or nearly half – of Colombia's municipalities didn't have a single police officer. People left those towns in droves – the second highest such exodus in the world. Most moved into the big cities, resulting in additional social problems.

Promising improvements

Today public police forces, judges and ombudsmen are in place to help maintain law and order. A recent report indicates that kidnappings have declined 22 per cent year-over-year and pipeline attacks have fallen, on average, 60 per cent annually. Health and education facilities also improved, contributing to a slow but steady decline in the national poverty index over the past decade.

As security and social infrastructure improved, so did the country's economic fundamentals. GDP grew steadily, outdoing the Latin American average. Inflation fell to two per cent in 2009, its lowest level in 55 years. Colombia also has had a promising start to 2010, with manufacturing production increasing 4.5 per cent and oil and gas production close to four per cent in the first third of this year.

Girón frankly acknowledges that Colombia's civil strife and drug trafficking are still far from over. Unemployment also continues to be relatively high at about 12 per cent. But these problems are more manageable today thanks to the reforms in law and order.

"We encourage Canadian companies to approach doing business in Colombia without hesitation. There are many sources of advice for them to do so, from the government of Canada's and EDC's trade representatives, to our Embassy and Proexport staff in Toronto," says Girón.

He emphasizes that consultations with these agencies should be part of any company's due diligence when investing in operations outside the major cities. "For example, when planning oil and gas or mining exploration, it is very important to understand our laws and policies for these sectors; to be informed about which areas to avoid; and to respect locations of indigenous reserves."

Companies like Petrominerales Colombia Ltd., a majority-owned subsidiary of Canada's Petrobank Energy and Resources Ltd. of Calgary, have done their due diligence and are successfully doing business in Colombia.

"We encourage Canadian companies to approach doing business in Colombia without hesitation," says Ambassador Girón.

This past summer, EDC's Benoit participated in a visit to Petrominerales' oil fields with some 40 analysts and investors to gain a deeper understanding of how the company operates. "We all got a good sense of how lean and well-focused the company is and how quickly they are able to move from oil 'find' to production. What might have taken another such company two or three years, Petrominerales has done within a year," says Benoit.

Production increased 75 per cent in the first quarter of this year, compared to the same period in 2009. Today, Petrominerales is one of Colombia's largest independent oil producers and one of its most productive – with 18 exploration blocks and two incremental production contracts with Ecopetrol in Colombia. As of June 2010 the company declared an enterprise value of some $2.8 billion.

Given the company's track record including four consecutive years of production growth, EDC contributed US$30 million towards the renewal and increase of a large credit facility last December, with other international banks. Before providing this support, EDC also assessed Petrominerales' environmental, health and safety, and social policies and practices, and was satisfied with the results. "The line of credit in which EDC participated provides us with strong financial flexibility going forward," says Jack Scott, Chief Operating Officer of Petrominerales.

Scott emphasizes that Colombia offers a positive investment climate, including a good investment rating and fiscal reforms implemented since 2004. The reforms include the creation of a central regulatory authority (ANH) that administers new exploration lands, plus reductions in royalties and corporate tax rates. There are now over 80 oil and gas companies operating in Colombia.

This year, the World Bank ranks Colombia first in South America for ease of doing business, which takes into account such factors as dealing with construction permits, employing local workers and protecting investors.

Petrominerales too has its unique advantages: for instance, its proprietary air injection process for extracting heavy oil, called THAI™, has resulted in higher oil recovery with lower operating costs and faster execution times. It also improves environmental performance, using less water and emitting less greenhouse gas.

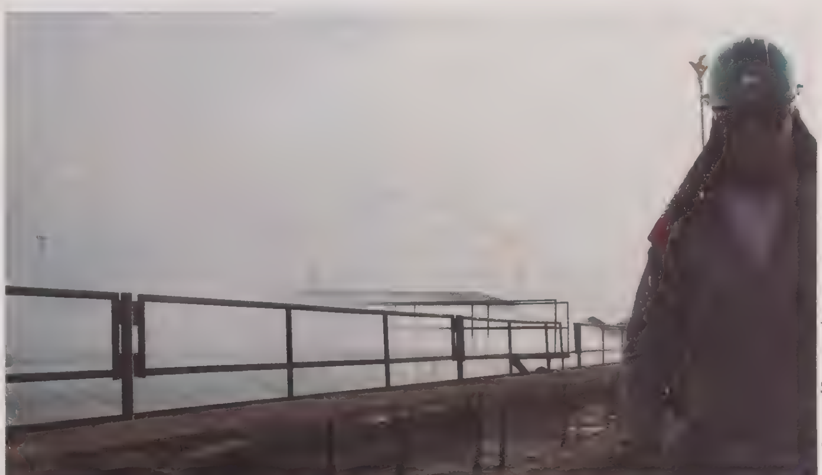

Photo: Courtesy of Petrominerales

Petrominerales oil and gas operations in the Corcel field in central Colombia.

Colombia is one of Canada's top markets for green lentils and imports **$70 million** worth of pulses a year.

In a different sector, Prime Seeds International Inc. is another Canadian company with a long and successful trading relationship with Colombia. "We have been exporting about 10 per cent of our products to Colombia for the last decade," says Ernesto Mejía, vice-president of this worldwide exporter of lentils, chickpeas, canary seeds, flax and beans. Headquartered in Vancouver, the company obtains most of its products from Saskatchewan.

"If you compare today with 10 years ago, it is much easier, much more secure, to move between different Colombian towns and cities to do business with our local clients," says Mejía, who is Colombian-born and travels to the country at least two or three times a year.

"Business in Colombia is based on good relationships – I have found this truer in Latin America than in many other parts of the world. So the best advice I can give is what I learned from my father when I was five years old – know your customer," says Mejía. This means understanding the language, the culture and taking time to meet in person and learn about each other.

With long-term relationships intact, Prime Seeds was not seriously affected by the recession. "People need to eat and our products are a staple in Colombia and the rest of our 45 markets," says Mejía.

Rising pulses

Mejía adds that even with the company's healthy results, it insures all its exports with EDC. "It's like having earthquake insurance. It also lets us increase our line of credit and EDC is helpful in providing information on our markets," he says.

As Prime Seeds is well aware, Colombia is one of Canada's top markets for green lentils and imports $70 million worth of pulses a year, according to Carl Potts, Director of Market Development for Pulse Canada – an industry association that represents growers, processors and traders of pulse crops in Canada. Not surprisingly, the association lobbied hard for the FTA, noting that it will ensure Canada retains competitive access to Colombia by removing the possibility of tariff disadvantages.

Ambassador Girón adds that the FTA also provides greater export opportunities for other important Canadian agri-food products, such as beef, pork, apples, peaches and berries.

In everyone's favour is the easy relationship between the two countries. As Girón's term comes to an end this year, he reflects on how enjoyable his time in Canada has been. "Once you interact with the people here, you realize how much we have in common – especially the open, warm and friendly natures of both our people. Culturally, it is easy to do business with each other," he says.

"You also enjoy many of the values that we would like to see more of in Colombia – tolerance, respect for others' opinions, respect for the law, all in a multicultural and multiracial society."

Colombia has much to gain from growing trade with Canada, Girón adds: "The FTA is one of the best tools to continue to improve the situation in Colombia. It will help create more good quality jobs, and encourage more companies to respect international labour, environmental and human rights standards if they want to compete globally." Both parties have agreed, for example, to annually prepare a public report on human rights developments stemming from the FTA. This will promote not just trade in goods and services, but also social progress. ■

CLICK . . .

› **sbenoit@edc.ca**

› **petrominerales.com**

View from EDC's Political and Human Rights Risk Assessment Desk (PHRAD)

Jorge Rave, a PHRAD analyst for EDC and native Colombian, travelled to the country on a fact-finding mission this past spring. Here he touches on how Colombia is evolving in human rights and some of the challenges that remain.

Colombians tend to give a frank assessment of the situation in their country. Human rights, drug trafficking and violence are still the biggest issues on people's mind when they are thinking of investing in Colombia. For many years, according to the United Nations, the culture of illegality was so pervasive, it also permeated political and business attitudes.

As the Ambassador pointed out, there have been dramatic changes since President Uribe took office in 2002, including large-scale demobilization of paramilitary and guerilla forces. Most political violence is now in isolated rural areas and security no longer seems to be the first priority for Colombians.

For companies in the extractive sector, in particular, there are still serious security issues, such as the risk of extortion by private "security" services. But we are also seeing better security measures endorsed by the government, and more corporate social responsibility initiatives, including new mechanisms to address human rights grievances. Many multinational companies understand the need to gain cooperation from indigenous communities through consultation and dialogue long before embarking on a project.

The Colombian state also demonstrated a clear division of powers this year when the Constitutional court ruled it would not be constitutional for President Uribe to run for a third term. This led to former Defense Minister Juan Manuel Santos winning the presidential election in June. He promised to maintain the previous administration's security policies, but will also need to concentrate on strengthening the economy and re-establishing diplomatic ties with Venezuela and Ecuador.

Another plus for business is that education and skill levels in Colombia are relatively high compared to many other Latin American countries. The government has a big task ahead to reintegrate the demobilized forces into the workforce, so they don't fall back into old patterns.

The situation in Colombia is still fragile, but the momentum is there for greater improvements in security, human rights and the economy as a whole.

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› **jrave@edc.ca**

Peter Hall Vice-President and Chief Economist

India: Building the Future Now

Landing in New Delhi after midnight on a steaming hot night in early April, and hopping a late-night ride to the hotel along traffic-choked boulevards lined with bustling markets alive with shoppers, merchants and passersby, my first impression was: "Recession? What recession?" That impression was further confirmed over the following four days as we travelled those same thrumming, traffic-snarled streets from one busy venue to another. Again, I had the same impression during my two-day stint in Mumbai. And, most importantly, it was corroborated and augmented in a series of meetings with policymakers, business operators and market analysts throughout my entire visit to India. From visible activity to verbal accounts, the message was the same: "Recession? What recession?"

And, that sentiment has a solid foundation in facts. Growth did slow during the global recession, but the weakest quarter saw a 5.8 per cent increase – impressive, to say the least. In the three quarters that preceded my visit, growth averaged just under eight per cent, making that quick dip a distant memory. In fact, at the current pace, growth has created another problem: soaring inflation. Consumer prices reached a 10-year high of 16.2 per cent in January. Since then, growth has edged back under 14 per cent, but that pace is strong enough that the Reserve Bank of India is busy tightening monetary policy. Interest rates have risen by 75 basis points so far this year, and more near-term hikes are likely in store.

How did India manage to escape the mayhem in the rest of the world? First, India's exposure to the rest of the world is lower than for the average emerging market. Trade as a share of GDP is just 46 per cent, compared with China at 70 per cent. India felt the impact when world trade collapsed late in 2008, but the momentum of consumer spending and private investment shielded its economy from the worst effects. In addition, monetary policy was very responsive to the downturn. But a key reason behind India's resilience is its pre-recession stimulus plan: the heavy ongoing investment in public infrastructure.

Policymakers in India are keenly aware that poor infrastructure is a key growth inhibitor, and as a result, attention has been paid to infrastructure spending in most of the more recent five-year plans. The current plan earmarked US$500 billion for various projects, from telecommunications to energy and transportation systems. India has been increasingly looking for private sector participation, with the targeted private component moving to 36 per cent in the current plan from 25 per cent in the 10th plan. From the new airport terminal and mass transit system in New Delhi to highways and other key projects, the evidence of the heavy public commitment to infrastructure renewal is visible everywhere.

"The Prime Minister and senior government officials have endorsed a whopping US$1 trillion in infrastructure monies."

Not content with today's substantial sums, the government has again upped the ante for infrastructure spending. In a preview of the 12th five-year plan (2012–17), the Prime Minister and senior government officials have endorsed a whopping US$1 trillion in infrastructure monies. If successfully dispensed, the program could go a long way to alleviating some of the more substantial encumbrances to long-term growth. Significantly, the upcoming plan recognizes India's inability to completely self-finance its immense projects, and the doors have been opened wider to capital inflows and partnership support from around the world.

In India, politics frequently gets in the way of the best laid plans. But recent developments suggest improvement on this front. First, federal governments appear to have become more stable. The last two governments managed to serve out their full terms, the first back-to-back complete terms since 1967. Second, in May 2009 the incumbent party was returned to power after serving a full term, again the first time this has occurred since 1967. Third, in those latest elections, the Congress-led United Progressive Alliance strengthened its hand considerably, with Congress alone winning 206 of the seats. This outcome cheered India-watchers, as it marked a notable defeat for reform-averse parties, and cleared the path for advancement of the economic growth policy agenda.

Furthering this agenda is critical to India's economic growth path. Recent success has given the country a taste for faster growth and its benefits, and the rich resources it possesses suggest that rapid growth is sustainable there for a longer period of time than anywhere else on the planet. But the inadequate infrastructure that has long restrained this economic powerhouse again threatens to undermine the achievable, aggressive growth trajectory, returning India to mediocre performance. Simply put, it's a key pivot point between success and stagnation.

Canada has great opportunities in India. Our presence there is growing: in the good years, exports rose 30 per cent annually, bringing two-way trade to $4.5 billion in 2008. Direct investment in India surged at the same time, rising 13 per cent annually to $801 million in 2008. This, together with Canada's international expertise in power systems and transportation infrastructure, suggests that Canada is positioned to participate in meeting India's needs. This is recognized in India, and is being supported by movement toward a bilateral nuclear agreement and negotiations toward establishment of a Canada-India Foreign Investment Promotion and Protection Agreement (FIPA).

The bottom line: India is on the march, and there is a growing determination to further the progress that has been achieved to date. This is well articulated in policy circles, and it's also obvious at street level. Putting critical infrastructure into place is key to realizing sustained, strong growth, and India is looking for international partners that can add to domestic capacity. Canada has the presence, the people and the products to be a player for a long time to come in this dynamic market. ■

CLICK ...
› **phall@edc.ca**

EDC Toolkit

EDC offers a wide range of trade finance solutions to Canadian companies and their customers abroad. The following summary is intended to act as a guide. Visit us online at edc.ca or call a small business representative at 1-888-332-9398, weekdays, 8 a.m. to 6 p.m. EST.

INSURANCE

Are you sure your U.S. or foreign customer will pay?
Don't risk it. Get EDC Accounts Receivable Insurance and we'll cover up to 90 per cent of your losses if your customer doesn't pay.

Do you know what the future holds for your investments abroad?
Use EDC Political Risk Insurance and protect your investments abroad from unforeseen political and economic upheaval. We'll cover up to 90 per cent of your losses.

What if my buyer calls my bond even though I didn't do anything wrong?
Protect yourself with EDC Performance Security Insurance which covers 95 per cent of your losses on a wrongful call or a call resulting from events outside your control, such as war.

For information on these and other insurance products, visit **edc.ca/insurance**.

WORKING CAPITAL

Do you need access to more financing?
By providing a guarantee to your financial institution through our Export Guarantee Program, we can help you access additional financing for export-related activities and/or foreign investments.

Do you need protection against currency fluctuations?
Do you purchase forward contracts from a financial institution to protect your cash flow against currency fluctuations? EDC's Foreign Exchange Facility Guarantee (FXG) can help. FXG frees up your working capital by foregoing a financial institution's requirement to put up to 15 per cent collateral on forward contracts.

With FXG, you can pay your suppliers up front without fear of losing money due to currency fluctuations.

For information on these and other working capital solutions, visit **edc.ca/wcs**.

ONLINE SERVICES

Will your customer pay?
Get a credit profile for as little as $30 with EXPORTCheck. We have more than 100 million companies in our database.
edc.ca/exportcheck

Looking for information on export finance?
The EXPORTFinanceGuide centralizes information about the financing tools and services available for Canadian exporters at various stages of the transaction cycle. **edc.ca/efg**

Want some market insight that will actually help you make a decision?
Check out EDC's Country Information – economic reports that monitor political and economic events and gauge opportunities in more than 200 markets. **edc.ca/e-reports**

Online Solutions Advisor
EDC's Online Solutions Advisor gives you fast and convenient access to information about which of our solutions may help you. Take a few minutes to answer questions about your export status, and get a diagnostic summary outlining potential EDC solutions available for your exporting needs.
edc.ca/advisor

Are you ready to enter the export market?
Test your readiness by completing EXPORTAble?, an online questionnaire to help you prepare for your entry into foreign markets.
edc.ca/exportable

FINANCING

Want to turn your export sale into a cash sale?
EDC offers a range of financing solutions for foreign buyers of Canadian capital goods and related services. Generally, our financing solutions provide one- to 10-year coverage for up to 85 per cent of the value of your sale.

EDC also has pre-arranged Lines of Credit with foreign banks, institutions, and purchasers under which foreign customers can borrow the necessary funds to purchase Canadian capital goods and services.

In partnership with Northstar Trade Finance, EDC can also provide fast and efficient medium-term foreign buyer financing for smaller capital goods export transactions. **northstar.ca**

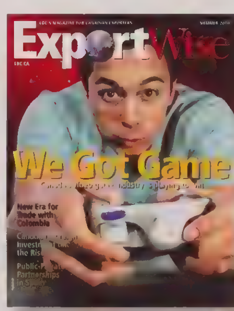
For information on these and other financing products, visit **edc.ca/financing**.

BONDING

What if my buyer demands a bond?
You can get bonds issued by either your bank (standby letters of credit or letters of guarantee) or a surety company (surety bonds). EDC can help you get those bonds by issuing a guarantee to your bank or by providing up to 100 per cent reinsurance to your surety company.

For information on these and other working capital solutions, visit **edc.ca/bonding**.

Check out *ExportWise* online at exportwise.ca



Trade Resources

A list of associations and government agencies dedicated to helping Canadian businesses succeed.

PROVINCIAL GOVERNMENT AGENCIES

ALBERTA
Trade Team Alberta:
alberta-canada.com/tta
TTA is a partnership of the Governments of Canada and Alberta, working to enhance international business opportunities for Albertans.

MANITOBA
MTI: Manitoba Trade and Investment:
gov.mb.ca/trade
MTI's mission is to help build the Manitoba economy through increased exports and by attracting and retaining foreign direct investment.

NEW BRUNSWICK
Business New Brunswick – Export Development Branch:
gnb.ca/0398/export/index-e.asp
Business New Brunswick's Export Development Branch specializes in counselling and other services to export-ready companies and existing exporters.

NEWFOUNDLAND AND LABRADOR
gov.nf.ca/doingbusiness
A gateway to online information for business, start-up, operations, relocating to the province, investments and exporting.

NOVA SCOTIA
Nova Scotia Business Inc.:
novascotiabusiness.com
NSBI offers many export development programs and services for small to medium-sized businesses and local exporters entering new markets.

ONTARIO
International Trade Development:
ontarioexports.com
The International Trade Branch of the Investment and Trade Division helps Ontario firms grow, prosper and create jobs through international trade.

PRINCE EDWARD ISLAND
PEI Business Development:
peibusinessdevelopment.com
The Trade, Marketing and Communications Division is responsible for the identification and pursuit of trade and export opportunities for Prince Edward Island business.

QUEBEC
Services for businesses:
entreprises.gouv.qc.ca
Information for investors, immigrants, entrepreneurs and future exporters of Quebec.

Investissement Québec:
investquebec.com/en
Financing products range from work for companies, cooperative businesses and non-profit organizations from start-up, expansion, export, R&D activities, to mergers and acquisitions.

SASKATCHEWAN
STEP: Saskatchewan Trade & Export Partnership:
sasktrade.sk.ca
STEP was created to provide trade development, custom market research and access to export financing for exporters in the province.

BRITISH COLUMBIA
British Columbia Asia Pacific, Trade and Investment Division, Ministry of Technology, Trade & Economic Development:
gov.bc.ca/tted
Assists BC companies to enter international markets and attracts foreign investment to BC.

FEDERAL GOVERNMENT AGENCIES

Business Development Bank of Canada (BDC):
bdc.ca
BDC plays a leadership role in delivering financial, investment and consulting services to Canadian small businesses, with a particular focus on the technology and export sectors of the economy.

Canada Business:
cbsc.org
Canada Business reduces the complexity of dealing with various levels of government by serving as a single point of access for federal and provincial/territorial government services, programs and regulatory requirements.

Canadian Commercial Corporation (CCC):
ccc.ca
The CCC serves as an effective Canadian trade instrument, bringing buyers and sellers together and closing successful export contracts on the best possible terms and conditions.

Forum for International Trade Training
fitt.ca
FITT equips individuals and businesses with the practical skills they need to succeed in today's competitive global marketplace.

Foreign Affairs & International Trade Canada:
international.gc.ca
DFAIT supports Canadians abroad; helps Canadian companies succeed in global markets; promotes Canada's culture and values; and works to build a more peaceful, secure world.

Team Canada Inc.:
exportsource.ca
Team Canada Inc's website is Canada's most comprehensive source of information and practical tools for new or experienced exporters.

ASSOCIATIONS

Canadian Manufacturers and Exporters:
cme-mec.ca
Canada's largest trade and industry association, CME promotes the continuous improvement of Canadian manufacturing and exporting through engagement of government at all levels.

Canadian Chamber of Commerce:
chamber.ca
As the national leader in public policy advocacy on business issues, the Canadian Chamber of Commerce's mission is to foster a strong, competitive, and profitable economic environment that benefits not only business, but all Canadians.

Canadian Federation of Independent Business:
cfib.ca
CFIB has been a big voice for small business for 35 years with 105,000+ members nationwide in every sector.

Canadian Association of Importers and Exporters
importers.ca
I.E. Canada represents and educates importers and exporters and advocates on their behalf to influence change. Membership includes importers, exporters, distributors and agents as well as custom brokers, lawyers, accountants, freight and shipping companies, airlines, banks and foreign trade promotion offices.

ExportWise

Executive Editor
Derek Ferguson, Director, Public Affairs,
dferguson@edc.ca

Editor
Michael Toope, mtoope@edc.ca

Managing Editor
Terri-Sue Buchanan, tbuchanan@edc.ca

Online Editor
Lisa Turriff, lturriff@edc.ca

Creative
Insight Communications

Translation
Provided by EDC's translation team, under the direction of Josée Lamirande and Joanne Durocher.

Contributors
Eric Beauchesne
Peter Hall
Toby Herscovitch
Dennis Jones
Sandi Jones
Danny Kucharsky
Eric Siegel
Kathryn Young

Printing Services
The Lowe-Martin Group

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EDC is a Crown corporation that provides trade finance and risk management services to Canadian exporters and investors in up to 200 markets worldwide.

All dollar amounts indicated are in Canadian dollars unless otherwise specified.

Ce document existe également en version française sous le titre Exportateurs avertis.

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Contacts

EDC REGIONAL OFFICES AND INTERNATIONAL REPRESENTATIONS

Head Office

Export Development Canada
151 O'Connor Street
Ottawa, Canada K1A 1K3
Tel.: 613-598-2500 | Fax: 613-237-2690
edc.ca

WESTERN

contactwest@edc.ca
Linda Niro, Regional Vice-President

Vancouver Office
Tel.: 604-638-6950 | Fax: 604-638-6955

Edmonton Office
Tel.: 780-702-5233 | Fax: 780-702-5235

Regina Office
Tel.: 306-586-1727 | Fax: 306-586-1725

Calgary Office
Tel.: 403-537-9800 | Fax: 403-537-9811

Winnipeg Office
Tel.: 204-975-5090 | Fax: 204-975-5094

ONTARIO

contactontario@edc.ca
Albert van Eeden, Regional Vice-President

Toronto Office
Tel.: 416-640-7600 | Fax: 416-862-1267

Mississauga Office
Tel.: 905-366-0300 | Fax: 905-366-0332

London Office
Tel.: 519-963-5400 | Fax: 519-963-5407

Ottawa Office
Tel.: 613-597-8523 | Fax: 613-598-3811

Windsor Office
Tel.: 519-974-7674 | Fax: 519-974-9753

QUEBEC

contactquebec@edc.ca
Diane Dubé, Regional Vice-President

Montreal Office
Tel.: 514-908-9200 | Fax: 514-878-9891

Quebec City Office
Tel.: 418-577-7400 | Fax: 418-577-7419

Drummondville Office
Tel.: 819-475-2587 | Fax: 819-475-2408

Ville Saint-Laurent
Tel.: 514-215-7200 | Fax: 514-215-7201

ATLANTIC

contactatlantic@edc.ca
David Surrette, Regional Vice-President

Halifax Office
Tel.: 902-442-5205 | Fax: 902-442-5204

Moncton Office
Tel.: 506-851-6066 | Fax: 506-851-6406

St. John's Office
Tel.: 709-772-8808 | Fax: 709-772-8693

MEXICO & CENTRAL AMERICA

Mexico City
Johane Séguin, Chief Representative
Tel.: 011-5255-5387-9316 | jseguin@edc.ca

Nathan Andrew Nelson, Regional Manager
Tel.: 011-5255-5387-9319 | nnelson@edc.ca

Monterrey
Marcos Pruneda, Regional Manager
Tel.: 011-5281-8378-0240 ext. 3360
mpruneda@edc.ca

Panama
Alain Gauthier, Chief Representative
Tel.: 011-507-294-2526
agauthier@edc.ca

BRAZIL & SOUTHERN CONE

São Paulo
Jean Cardyn, Regional Vice-President, South America
Tel.: 011-5511-5509-4320 | jcardyn@edc.ca

Monica Busch, Regional Manager
Tel.: 011-5511-5509-4361 | mbusch@edc.ca

Rio de Janeiro
Fernanda de A. Custodio, Regional Manager
Tel.: 011-5521-2295-0391 | fcustodio@edc.ca

ANDEAN REGION

Lima
Stephen Benoit, Chief Representative
Tel.: 011-51 1 319-3385 | sbenoit@edc.ca

CHILE

Santiago
Christian Daroch, Regional Manager
Tel.: 011-56 2 652-3807 | cdaroch@edc.ca

CENTRAL EUROPE

Warsaw (Poland)
Marzena Koczut, Chief Representative
Tel.: 011-4822-584-3240 | mkoczut@edc.ca

GREATER CHINA

Shanghai
Jacques Lacasse, Chief Representative
Tel.: 011-86-21-32792832 | jlacasse@edc.ca

Beijing
Wang Hui, Associate
Tel.: 011-86-10-51394126 | hwang@edc.ca

RUSSIA AND CIS

Moscow
Rod Lever, Chief Representative
Tel.: 011-7 495 925-6095 | rlever@edc.ca

John Place, Chief Representative
Tel.: 613-598-2869 | jplace@edc.ca

Maxim Berdichevsky, Regional Manager
Tel.: 011-7-495-925-6896 | mberdichevsky@edc.ca

SOUTHEAST ASIA

Singapore
Peter Nesbitt, Regional Vice-President, Asia
Tel.: 011-65-6854-5868 | pnesbitt@edc.ca

Rob Simmons, Chief Representative
Tel.: 011-65-6854-5949 | rsimmons@edc.ca

INDIA

New Delhi
Vibhav Agarwal, Regional Manager
Tel.: 011-91-11-4178 2288 | vagarwal@edc.ca

Mumbai
Rajesh Sharma, Regional Manager
Tel.: 011-91-22-6749-4480 | rasharma@edc.ca

Vijendra Gairola, Chief Representative, India
Tel.: 613-597-8594 | vgairola@edc.ca

UNITED ARAB EMIRATES

Abu Dhabi
Jean-François Croft, Chief Representative
Tel.: 011-971-2-694-0376 | jcroft@edc.ca

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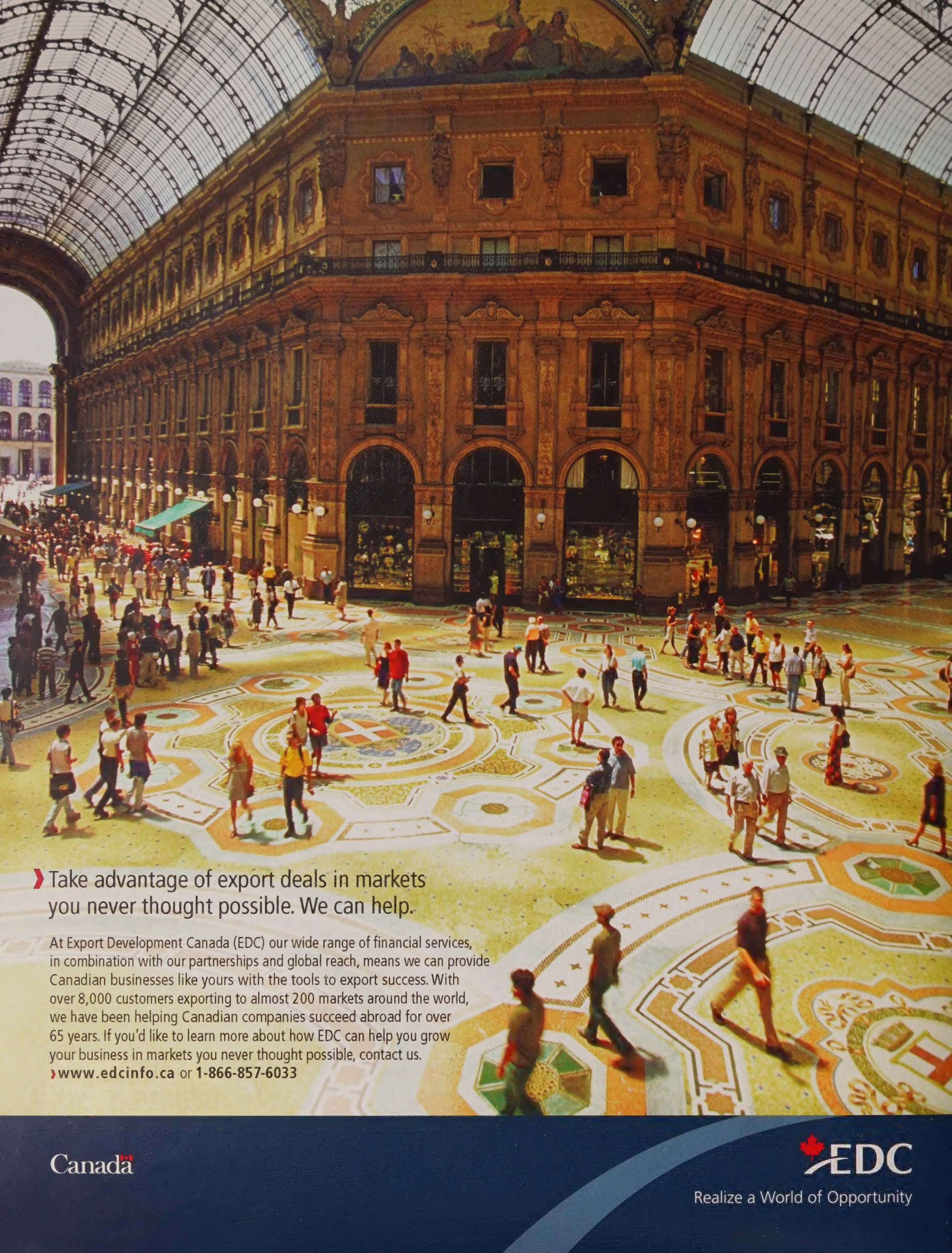
Companies with total **annual sales of more than $10 million** can call the nearest EDC regional office at **1-888-332-3777**.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